Contingency Plans: Helping a Spouse Cope Financially After Your Death

By Maria Crawford Scott

Florence and Norman Stone are both in their late 60s and enjoying their retirement years. During their working years, Norman had spent long hours building up a small dental practice, which he closed down several years ago. Florence stayed at home with their two children while they were small, but returned to teach school when the children were older. She retired from her teaching, though, when Norman closed his business down.

Florence has always managed their financial assets, and she continues to do so now. Their current portfolio consists of both taxable accounts and two IRAs, one Norman's and a smaller one belonging to Florence. In addition, Florence receives a pension from her teaching position. Currently, it pays annuity benefits of about $20,000 a year; it is a joint-and-survivor's annuity, with reduced payments to Norman should Florence die first.

Norman has never taken much interest in their financial affairs—in fact, he dislikes the whole topic. Florence, on the other hand, has always been interested in picking her own stocks, having gotten her start years earlier in an investment club. She now manages a portfolio of about 10 smaller-capitalization stocks. Florence also invests in mutual funds that she thinks are well-managed and good complements to their individual stock holdings. She has invested Norman's IRA in a fund that focuses on high-quality larger-capitalization companies; her own smaller IRA is invested in an aggressive growth small-cap fund. Their remaining taxable assets are invested in an equity-income fund, an international fund, an intermediate-term bond fund, and a money market fund.

At first glance, it may appear that the Stones are very heavily committed to stocks, with 80% of their non-pension assets invested in equities and 20% in fixed-income and cash. However, in determining their desired allocation, Florence takes into consideration the pension payments she receives, which she treats as a fixed-income asset. By taking the pension payments into consideration, their current allocation changes quite a bit—they are now 60% invested in equities, and 40% invested in fixed-income and cash.

The current allocation provides the Stones with a steady source of income to meet living expenses, as well as a source of growth should their living expenses rise due to inflation. Florence is also comfortable with the uncertainty surrounding the market's outlook; she feels that their portfolio's diversification will help dampen volatility, and allow them to ride out the downturns in any market segment.

Recently, Florence began to realize that although she has dealt with market uncertainty, she hasn't really thought much of other uncertainties—in particular, how the asset allocation strategy may change should she die. The Stones do have wills, and Florence has thought through several estate planning issues. But she hadn't thought much about what Norman would need to do if he were left on his own. After all, she is the one who maintains the portfolio, and keeps it in line with the strategy. In addition, if she were to die, the pension payments would be cut, altering the allocation mix. Then she started thinking of other problems:

- He could receive his survivor's benefits from her pension in the form of a lump-sum distribution. Would he know how to analyze his options and know where to invest the proceeds?
- Would he know what to do with the proceeds from her IRA?
- Would he know how to monitor the actively-managed mutual funds that they hold?
- Norman really knows nothing about investing in individual stocks, much less the rationale behind her current stock picks. How, then, would he manage the portfolio of small-company holdings that they now own?

- Would Norman know when not to sell funds or stocks—for instance, if his life expectancy is very short and he could pass on to their children an asset with big unrealized gains on a stepped-up basis?

Florence is also concerned because some of these decisions may need to be made at a particularly emotional time for Norman, closely following her death. And even if it isn't necessary to make these decisions soon after her death, Norman may feel pressured to do so—despite the fact that Florence manages their finances, Norman gets plenty of calls from salespersons pitching one financial product or another, and he is too polite to hang up quickly.

On the other hand, Florence can't plot out the rest of Norman's life without her. She has no idea of what his needs would be, particularly since his life would change so dramatically. In short, he is most likely going to have to reconsider his asset allocation strategy as best he can after he has had time to adjust to her death.

Florence decides that the best contingency plan is to leave Norman with a well-organized file that contains information he will need, including some suggestions on what to do in certain situations; and to discuss it with Norman so he is familiar with its contents and suggestions.

The file includes a list of all of their financial assets, including the financial institutions where they are held, their account numbers and how they are titled; information on who to contact concerning Florence's pension; and a list of advisors Florence has used in the past (an accountant and a financial planner who helped Florence with some estate planning questions).

The file also includes some suggestions on how he may want to handle his finances upon her death. It is designed to give him a course of action he can follow during the emotional time period immediately following her death, and tide him over until he can make longer-term decisions once he has a better idea of his future needs:

- After talking with Norman and analyzing the options, Florence suggests that he will most likely want to continue with the pension payments. But she provides him with a possible advisor should he need help analyzing the options.
- Other assets he may receive upon her death (such as life insurance payments) should be invested in short-term fixed-income funds. This will provide Norman with liquidity should he decide at a later date that he wants to invest elsewhere. Florence provides a list of several funds that she considers to be good candidates.
- Her IRA can be rolled over into his IRA, investing it in the same aggressive growth fund so that the asset allocation remains unchanged until Norman has a better idea of his needs.

Florence then discusses the file with Norman, explaining how their assets are invested and her current strategy, and providing tips he may want to consider in the future if he is ever on his own. She points out the advantages of mutual funds, and notes that index funds are a good alternative for someone who doesn't know much about mutual fund selection. Thus, if Norman is uncomfortable judging the merits of an active manager, he could consider the index alternative. Florence warns Norman, however, of the tax consequences of selling funds in their taxable accounts, and also notes that there may be some estate planning questions that may arise. She points to the list of advisers that Norman can contact should he need more specific advice.

She also suggests that Norman may want to seek help in managing the portfolio of individuals stocks, and she again points out the list of possible advisors.

Lastly, Florence makes a point of discussing the contingency plans with their children, so that they can provide their father with assistance if necessary.

The Best Plan: A Short-Term Bridge

The death of a spouse is clearly going to be a trying and emotional time for the survivor. But it will be particularly hard if the surviving spouse is unfamiliar with the family finances. If you are managing the finances, the best contingency plan, of course, is to familiarize your spouse as much as possible with your investment approach.

Here are some other contingency-planning thoughts to keep in mind :

- While some suggestions can be made, the death of a spouse will dramatically change the lifestyle, income needs, and income sources of the survivor. That will necessitate a reassessment of their financial situation, including the asset allocation strategy. This cannot be anticipated in advance, and should be done once the survivor has adjusted to the new situation.
- Financial decisions should be put off until the surviving spouse has had a chance to reconsider their financial needs and circumstances. Until that time, it would be useful for them to have a list of suggested short-term mutual funds in which to park newly received assets, such as life insurance payments or lump-sum pension distributions, until a final decision can be made.
- Advisors may be needed to provide expertise in areas in which the spouse is particularly unknowledgeable, such as managing or disposing of a portfolio of individual stocks, whether to take lump-sum distributions, and in tax and estate planning questions. If you can provide a list of people you think would be helpful, or even the type of advisor to seek for different areas, it would be a head start.
- While you should discuss the contingency plans with your spouse, they should also be written down. Memories are faulty, particularly during emotional time periods. And as all of us who are married know, spouses are not always the best listeners.
- You may also want to include a list of "things that need to be done" following the death of a spouse.

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