Chicago Daily Law Bulletin®

Volume 162, No. 210 Serving Chicago's legal community for 161 years

Financial literacy: The hidden, but vital part, in divorce law practice

The financial component of divorce cannot be understated.

The outcome of a divorce will impact an individual's financial future in immense ways.

Even so, I have seen firsthand in my work how some people don't truly understand their finances. I have encountered clients with varying degrees of financial literacy.

In those situations especially, having a lawyer that understands finances and is able to educate a client to understand their finances is invaluable. Understanding finances is empowering for clients.

Financial literacy is a term that is often used in the world of personal finance, but what exactly does it mean to be "financially literate"? And more important, why does it matter whether or not you are financially literate?

To answer the first question, financial literacy is an individual's knowledge base and corresponding ability to understand and manage their money in an efficient manner. It is the ability to understand how one spends their own money as well as how to deal with decision-making, budgeting and planning for one's own financial future, including saving and investing.

As for why it matters, financially literate people tend to make more sound decisions regarding their money, and as a result, benefit from the positive impact those decisions have down the road.

Financially literate people understand concepts like compounding interest, the time value of money, the impact of taxes and debt management and they are able to track their spending, budget and invest. A person's financial literacy level impacts their attitudes and behaviors when it comes to money, particularly saving and spending that money.

A financially literate person typically doesn't live beyond their means, plans for the long term and is better off when facing the inherent issues that arise in life through no fault of their own, such as illness, job loss or market downturns.

However, studies have shown many people are financially illiterate. I recently reviewed a study by the Organisation for Economic Co-Operation and Development and the International Network on Financial Education and the results were troubling, to say the least.

The study, "OECD/INFE International Survey of Adult Financial Literacy Competencies," examined 30 countries and economies throughout the world and found that "overall levels of financial literacy are relatively low."

In the study, the average score was 13.2 out of a possible 21 points, and France, which had the highest score, was only 14.9, which, as the study put it, "shows significant room for improvement."

A financially literate person typically doesn't live beyond their means, plans for the long term and is better off when facing the inherent issues that arise in life through no fault of their own, such as illness, job loss or market downturns.

MODERN FAMILY

Patrick T. Ryan

Patrick T. Ryan is a partner at Schiller, DuCanto & Fleck LLP whose practice concentrates on resolving complex family law and divorce cases, both through negotiation and litigation. As a certified financial planner professional, Ryan helps clients to understand their current personal financial situation and plan for their financial future. He can be reached at pryan@sdflaw.com.

Other findings include:

• Only 56 percent of adults achieved the minimum score to be considered financially literate.

• Only 42 percent of adults were aware of the benefit of compounding interest.

• Only 58 percent could calculate simple interest on savings.

• 33 percent of people were unaware that it is possible to reduce investment risk through diversification.

• In terms of financial behavior (budgeting, planning and investing), only 51 percent achieved the minimum target score to be considered financially literate.

• Long-term financial goal setting and planning is not common in many countries.

Perhaps a more striking finding was the difference between genders — 61 percent of men were able to achieve the minimum target score of financial literacy, compared with only 51 percent of women.

That number changes slightly when focusing on countries that are typically considered to be more advanced, but even then, 69 percent of men were able to reach the minimum score, compared to only 56 percent of women.

The countries in the study included France, Canada, the United Kingdom, Norway and Brazil, to name a few, and while the United States did not participate, it would be hard to believe that our results would be much better.

In June, the Financial Industry Regulatory Authority released a study where they found 61 percent of people were unable to pass a basic financial literacy test and only 37 percent were considered to be financially literate, which is even lower than previous studies in 2012 (39 percent) and 2009 (42 percent).

While the findings are troubling, perhaps they are not completely surprising. Money is so important in everyone's daily lives, yet we are so secretive about it.

We typically don't talk about budgets, savings and investment strategies with our friends. In fact, many feel that personal finance is a taboo social subject. As a society, we do not put a strong emphasis on basic personal finance education and while that has been improving recently, there is still a long way to go.

In a divorce, being financially literate is crucial to help clients set aside emotions and ego and empower them to make sound decisions for the future. It enables them to understand and more actively participate in the decisions being made now, which will inherently impact them for the rest of their lives.

More important, that financial literacy can be taken beyond the divorce and into the future, to help them provide for their needs and the needs of their family for years to come.