SPECIAL NEEDS PLANNING

By

PAULA L. PEADEN, ESQUIRE
Parker, Pollard Wilton & Peaden, P.C.
6802 Paragon Place, Suite 300
Richmond, VA 23230
(804) 261-7326
www.ppeaden@parkerpollard.com

I. INTRODUCTION

A. There are two crises which may be imposed upon us - total disability, and terminal illness. A third we all face - death.

B. Each crisis often has a heavier impact on our loved ones than on us. The need to prepare for each will often determine whether the crisis is an affliction or an opportunity for growth.

C. Many parents with disabled children worry a great deal about what will happen to their child if the parent becomes unable to care for them.

II. WILL

A. Burdens imposed by the lack of a will.

1. Judge decides who will be the administrator of your estate and the guardian of your minor or incapacitated beneficiaries rather than you.

2. Administrator cannot sell real estate without Court approval.

3. A costly and burdensome guardianship must be established for minor or incapacitated beneficiaries Inheritance is not protected!

a. Annual costs - fees to attorneys; premium to bonding company; cost of court proceedings, if required for approval of use of funds; fee to Commissioner of Accounts

b. Complicated accounting required yearly of receipts and disbursements.

4. Only in a will can you name a standby guardian for your minor child.

B. A homemade (Holographic) will is dangerous.

1. Ambiguous, unclear language in will promotes expensive and unnecessary lawsuits to interpret will.

2. Your property may pass to people you do not want to be your beneficiaries.

3. Do not try to change the will prepared by your attorney by handwritten provisions - may void will.

4. Need for a self-proving certificate.

C. Jointly owned property is a poor answer to certain problems.

1. The joint owner may appropriate the property to his own use contrary to the wishes of the other joint owner. Can disrupt your estate plan. Property that is owned jointly with another passes without regard to your will. If you hold property jointly with one child that property passes to that one child regardless of what your will says. Also, if you have named one child and they predecease you, the property may be distributed in accordance with the intestate laws which may or may not be what you want.

2. Could lead to costly and cumbersome guardianship. By having your funds paid under your will or under a trust, you can provide that if one of your children predeceases you, their share is to be held in trust for their children. You can designate at what age you want your grandchildren to receive the money outright

3. The surviving joint owner may be incapable of proper management of the property due to illness, incapacity or lack of experience.

4. Often litigation is required to determine whether right of survivorship was intended.

5. When parent places property in joint ownership with child, bad relationships with other children often result.

6. Holding property jointly with a spouse can cause estate taxes to be imposed by failing to use one of a married couple's two unified credits.

D. A simple will may hurt your loved ones.

1. May pay unnecessary estate taxes.

2. Federal estate tax credit shelters from taxation estates up to $2,000,000.00 in value.

3. Do you wish to provide for the simultaneous death of you and your primary beneficiary (spouse, relative, etc)?

4. Do you want your spouse's second marriage to cause a disinheritance of your children?

5. Controls disposition of property upon your death. Names an executor to administer your estate.

6. Should you set up a "Special Needs Trust" for a disabled spouse or child? This type of trust is designed to supplement public benefits without causing the disabled individual to be disqualified for public benefits.

III. Special Needs Trust.

A. Types of Special Needs Trusts

1. Funded with Disabled persons resources. The person may have received them as a result of a personal injury suit or may have been gifted the resources without proper planning.

a. Pooled Trust - A pooled trust is established and administered buy a non-profit organization. Each beneficiary has a separate account, but the funds are pooled for investment and management. At the death of the beneficiary, the trust must repay to the state an amount equal to the amount of assistance the beneficiary has received from the state. If the beneficiary has used all the funds then there is no repayment to the state. The trust must be irrevocable. The Pooled Trust is usually used when there is no trustee willing to serve and when the trust funds are small. A disabled individual may set up their own pooled account.

b. SNT Payback Trust - This is a trust that must be created for the sole benefit of the individual with a disability under the age of 65. The trust can be created by the individual's legal guardian, the court, the parent or the grandparent. At the death of the disabled person the state Medicaid agency will be "paid back", to the extent funds remain, any monies expended by the state on the disabled individual.

2. Third Party Special Needs Trust - This trust is used for funds gifted or bequeathed to a disabled individual by anyone, and does not have a payback provision.

B. Goals

The parents of a child who has special needs plan for the future by providing educational, therapeutic and vocational experiences designed to promote skills and abilities to maximize self-reliance and enjoyment of life. During their lifetime, parents directly influence the quality of their child's life. Special needs estate planning seeks to plan for the child's life when the parents are no longer in charge. A properly drafted trust can preserve resources but also insure a quality of life for the disable child and give peace of mind to the parents, regardless of the size of an estate.

C. What is a special needs trust? A trust which sets aside assets in a way so as not to interfere with governmental entitlements and benefits. This is an irrevocable, inter-vivos or standby trust which typically receives funds at the death of the parent.

The trustees are to use the income and possibly the principal of the trust to supplement the benefits and income provided by Medicaid, SSI, and other governmental aid programs.

The trust income is available for limited purposes ("special needs") to benefit the child. At the death of the child, the principal will be distributed to a named remainder person, often another child, the grandchildren or to a designated charity.

Some trusts specifically state that the trustee can make no distributions that will make the beneficiary ineligible for public benefits, and in particular, SSI and Medicaid. In most cases, this is an unnecessary and unwise limitation on the discretion of the trustee.

It is preferable for the trust grantor to only state a preference that the trustee not make distributions that would make the beneficiary ineligible for public benefits, but allow the trustee the discretion to make disqualifying distributions if the trustee sees fit to do so.

<u>Why?</u>

1. Because the corpus of the trust may have great dollar value, it is sensible to make distributions to the beneficiary even if it means the loss or reduction of public benefits.

2. The trustee may decide to make significant distributions to the beneficiary in one month, causing a temporary disqualification for public benefits. After a period of ineligibility, the beneficiary would again be eligible for public benefits.

3. The uncertainty of future eligibility requirements for SSI and Medicaid (as will as other present or future public benefits) argues for granting the trustee the widest possible latitude in making distributions.

4. The beneficiary's condition may improve enough so that he or she is no longer sufficiently disabled to qualify for SSI, Medicaid or other public benefits. (Or the legal standard of disability may change and so make the beneficiary ineligible.)

   Note that granting absolute discretion to the trustee supposes a sophisticated, knowledgeable trustee who will understand the implications of any distributions in light of the eligibility of the beneficiary for public benefits.

D. Examples of problems.

1. Grandfather sets up income only trust for disabled granddaughter. The principal is made non-invadable so "government can’t get it." Granddaughter is placed in a residential facility ideal for her needs. Grandfather dies and now income from trust makes her ineligible for Medicaid. Since the trust can’t be invaded for principal, the granddaughter loses residency.

2. Divorce agreement calls for support to be paid to a disabled child beyond his eighteenth birthday. $400 in support causes loss of more than $300 per month in SSI. Use of a trust would have avoided this.

3. SSI discovered that whole life insurance policies purchased by parents for their disabled child as an infant were valued at over $2,000. Therefore, SSI determined the child was never eligible and asked for refund of all years of payment.

E. Who should be in charge?

1. At least one should be a Virginia resident. If a living or standby trust is used the Trustee can be out of state.

2. Your spouse.

3. Your other children.

4. Your attorney.

5. Your bank.

6. Your fiduciary should follow your instructions in the documents to establish a foundation for decision-making based upon what parents would have done under similar circumstances.

IV. PROBATE

Probate is the court administration and oversight of your affairs at death. When an individual who owns property and has a will passes away, the probate rules require that the will be submitted to the local court.

A. Advantages of Probate

1. *Creditor Protection* - When an individual dies with a will, a specific time period is set by the court allowing the deceased person's creditors to make a claim against his or her estate.

2. *Cost* - The cost of a living trust is greater than the cost of a will. You also must retitle your assets into the trust. Although retitling your assets may be a time consuming process for you, it greatly simplifies the handling of your affairs for your family members. All of your assets are easily identified and located in the trust.

B. Disadvantages of Probate

1. *Expenses* - Probate may become expensive depending on the complexities involved in your estate. There are administrative fees due to court involvement. Due to the bureaucratic nature of the court system, processing your estate can take up to six months or even longer. Thus, all

of your heirs will have to wait out this time period before receiving the inheritance you have left them.

2. *Contest* - Unhappy relatives can contest the validity of a will during the probate process.

3. *Will Is A Public Record* - Since most court files are accessible to the public, your will and your estate will be available for the public's viewing. Thus, anyone can see the value of your estate and the names of your beneficiaries.

V. AVOIDING PROBATE

A. Living Trusts - The Living Trust is a tool used to accomplish:

1. Lifetime Family Protection

2. Probate Avoidance

3. Death Tax Reduction

The trust is called a "Living" trust, since it is used during the lifetime of its creators. The trust is "Revocable" to allow it to be changed or terminated at any time by its creator.

4. Key Advantages

a. *Disability*. The Living Trust will enable your substitute trustee to take over the management of your affairs, if you become disabled. The substitute trustee could see that all of your needs would be met, if you were unable to do so. You can set forth a plan for the management of your assets for a time when you are not acting as a trustee. You can set forth very specific provisions regarding your assets.

b. *Privacy of trust assets*. The funded Living Trust is a completely private document. It prevents the public from having any knowledge of the assets contained in the Living Trust.

c. *Avoids probate in several states*. If a creator of the trust owns property in several different states, the Living Trust avoids the necessity of probating the will in the several different states where real estate is located.

d. *Portability of trust*. In the event that the creator decides to move out of the State of Virginia, this Living Trust can be moved with the creator to any other location desired.

B. Additional Advantages For Married Couples

1. *Simplifies trust documents*. An alternative to the use of a revocable living trust agreement for the husband and a second revocable living trust agreement for the wife, in addition to a will for each person, is the Joint Living Trust.

2. *Ease in estate tax planning*. With proper estate planning, a married couple can own property valued up to $7,000,000 and have no estate tax after the deaths of both spouses. The most advantageous planning requires the couple with $7,000,000 to title $3,500,000 in property in each spouse’s name. The Joint Living Trust can greatly simplify titling the assets in the most beneficial way between the husband and wife.

VI. WHO NEEDS ESTATE TAX PLANNING?

A. What is included in determining the size of an estate for federal estate tax purposes?

Any asset you own including your personal property and life insurance.

Putting an account in joint names does not remove the funds from your federal taxable estate.

Although the marital deduction allows married couples to transfer an unlimited amount of assets between themselves tax free, the problem occurs when the second spouse (or surviving spouse) passes away.

B. *Credit Shelter Trust* (also referred to as "Family Trust" or "By-Pass Trust"). Used to take the best possible advantage of federal estate tax law. In essence, up to $5,000,000 from the estate of the first to die would go into the family trust. This would be available to the surviving spouse, as well as children, if needed for support, health and education. The assets going into the family trust would not be taxed in the estate of the first to die because each spouse is allowed to pass on up to $5,000,000 tax free. Looking further ahead, these funds would not be considered part of the estate of the surviving spouse and, therefore, would not be subject to estate tax. In that way, the survivor's estate would be significantly reduced, as would the taxes on that estate.

The annual exclusion rule does permit individuals to give away $13,000 per recipient, per year. Husband and wife can give $26,000 per donee each calendar year. But instead of relying on the surviving spouse’s ability to make gifts, the two unified credits should be used first, and then gifts can be made if further estate tax reduction is needed. As stated above, $10 million can be protected from estate taxes by using a credit shelter trust.

C. *Disclaimer Will.* Credit shelter trust could be created in a living trust or in a will. If a will used the tax protection would be achieved but probate would still be necessary. Individuals use this when it is not clear that they will exceed the unified credit amount.

D. *QTIP Trust.* An effective method to pass property to children, while permitting the surviving spouse to retain the benefits of that property for his or her lifetime and still qualify the property for the marital deduction.

E. *Life Insurance Trust. To avoid tax on life insurance:*

1. DO NOT be the owner of the policy.

2. DO NOT make your spouse the beneficiary.

3. AVOID Three-Year rule on transfer of policy ownership.

VII. DURABLE GENERAL POWER OF ATTORNEY - HIGHLY IMPORTANT ALTERNATIVE TO GUARDIANSHIP

A. The Total Disability Crisis. The Life Insurance industry tells us that 50% of the people in our country today will at some time in their life suffer from total disability for 90 days or more. If no pre-crisis planning has been done and the individual is no longer able to care for his or her affairs, many problems must be unnecessarily faced by the family or loved ones of the disabled person.

B. When Is A Guardianship Needed? If a mentally or physically disabled person is unable to make the decisions necessary to carry out the responsibilities of living and has done nothing, while competent, to designate a substituted decision maker, often it is necessary to have the court appoint a guardian to make these decisions for the incapacitated person.

C. Why Guardianship Should Be Avoided Whenever Possible. Substantial, unnecessary costs are incurred in having a court designate a guardian to manage the affairs of a disabled person. If real estate is owned by the disabled and has to be sold, a legal action must be filed seeking the court's permission to sell the real estate. The guardian has many costs to pay such as bond premiums, attorney fees and fees to the Commissioner of Accounts, all of which could have been avoided. Family harmony can be disrupted over which person should be designated the guardian. Often over $5,000 in unnecessary costs are incurred in a guardianship, none of which directly benefit the disabled.

D. Guardianship Often Is Demeaning To The Disabled. Usually the disabled must be declared incompetent by a court before a guardian can be appointed. The incapacitated person may in the process be deprived of the right to make all of life's decisions, even though he or she might be able to carry out certain responsibilities without help. Depriving the individual of the ability to make decisions and to do those things which that disabled person can do often causes the person to fall into deep depression, which in turn may cause early death or serious illness.

E. The General Power Of Attorney Is The Most Important Legal Document An Individual Can Have. Most people assume that a will is the most important legal document one can have. A General Power of Attorney is equally as important. It authorizes your agent to do practically any act which you could do for yourself.

F. Definitions

1. *Power of Attorney*. A legal document in which you designate another person to act for you.

2. *Principal*. When you have the power of attorney prepared for yourself, you are the Principal.

3. *Agent or Attorney-in-Fact*. The one you designate to act in your behalf is your Agent. The Agent under a Power of Attorney is also known as the Attorney-in-fact. The Agent can be an individual, a bank, or a corporation.

G. What Does The Word "Durable" In A Power Of Attorney Mean? It is highly important that the Power of Attorney state that its effectiveness will not terminate on the incapacity of the Principal. If this language is not included, the document will be terminated by the incapacity of the Principal.

H. Should The Agent Be Authorized To Make Gifts? The Principal may want to allow the Agent to make gifts to certain persons in order to avoid high death taxes or to express the Principal's concern for his loved ones. The specific power to make these gifts should be included in the Power of Attorney with whatever limitations the Principal wishes to impose. This gift giving power may cause serious tax problems to the Agent, if the Agent dies while the Principal is living. Sound legal advice can avoid unexpected tax traps.

I. Integrity And Trustworthiness Of The Attorney-In-Fact. The agent must be a responsible, honest, intelligent person, who can be trusted with the often heavy responsibilities of caring for the Principal. Untrustworthy, immature, or irresponsible persons serving as an Agent can do great damage to the estate of the Principal, whether or not disabled.

J. Premature Use Of The Power Of Attorney. Sometimes a relative or other person serving as the Agent under a Power of Attorney will begin to use the document before the Principal wants the Agent to act. Before the Principal knows what is happening, the Agent might have taken all responsibility for managing the estate of the Principal away against the wishes of the Principal. Such action is often highly detrimental to the morale and well-being of the Principal. Parker, Pollard & Brown offers an escrow service to its clients where it will retain possession of the power of attorney with a letter of instruction on when it can be used. Typically the escrow letter instructs the law firm to release the power of attorney only if, in the opinion of the law firm, the Principal is incapacitated. The escrow letter may release and indemnify the law firm for the release of the power of attorney. Such an arrangement can often avoid the premature use of the document.

K. Need For Experienced Legal Advice In Drafting. A General Power of Attorney is a document filled with pitfalls and potential family disasters, when prepared by one who is not a skilled attorney in estate and taxation law. Forms for this legal instrument can be found in form books or purchased at a stationary store, but the purchaser must beware, since the form may fail to do the job that is needed.

L. If your disabled minor child is mentally incapacitated you may need to file for guardianship and conservatorship when they approach their 18th birthday.

VIII. UNDERSTANDING THE LEGAL COMPONENTS OF ADVANCE DIRECTIVES

A. ***Definition of an Advance Directive***.

Virginia Code Annotated § 54.1-2982 defines an Advance Directive as "(i) a witnessed written document, voluntarily executed by the declarant in accordance with the requirements of § 54.1-2983, or (ii) a witnessed oral statement, made by the declarant subsequent to the time he is diagnosed as suffering from a terminal condition. . ."

1. <u>The written directive</u>. Virginia Code Annotated § 54.1-2983, requires a written statement by a competent adult "authorizing the providing, withholding or withdrawal of life prolonging procedures in the event such person should have a terminal condition". If the individual is incapable of making an informed decision, the directive may appoint an agent to make health care decisions for the declarant. The document must be signed in the presence of two witnesses, who are not related by blood or marriage to the declarant, who must also sign.

2. <u>The oral directive</u>. An oral directive may be made if the patient is in a terminal condition and the directive is made before the attending physician and two witnesses.

B. ***Definition of Declarant***.

An adult who makes an Advance Directive while capable of making and communicating an informed decision.

C. ***Definition of the Agent in the Advance Directive***.

An adult appointed by the declarant to make health care decisions for him.

D. ***What Should Declarant Do with the Advance Directive***?

1. The primary care physician is the most important person to have a copy of the Advance Directive. Any other physician should have a copy, when providing care to the patient for a condition that is or may become life threatening.

2. A copy of the Advance Directive should be given to a hospital, nursing home, hospice or home health care provider that is responsible for health care to the patient.

3. The agents under the Advance Directive should each have a copy.

4. The Declarant should discuss his/her wishes related to the Advance Directive with those receiving a copy in order to be certain the Declarant's wishes stated in the Advance Directive will be carried out.

5. <u>Photocopies of Directive</u>. The health care provider or other persons need not have a copy of the directive that has been personally signed by the declarant and witnesses. A photocopy of the document that has been personally signed is sufficient.

E. ***Necessity for the Declarant to Be Incapable of Making an Informed Decision***.

1. The Virginia Advanced Directive can become effective only when the declarant is incapable of making an informed decision.

2. For one to be incapable of making an informed decision under Virginia law, Virginia Code Annotated, § 54.1-2982, the following is required:

    a. The patient must be suffering from a mental illness, mental retardation, or other mental or physical disorder.

    b. This disorder must preclude communication or impair judgment, so that the patient can not make "an informed decision about providing, withholding or withdrawing a specific medical treatment.

3. The patient's attending physician and a second physician or licensed clinical psychologist, after personal examination of the patient, must certify in writing that the conditions in two preceding paragraphs above do exist prior to giving, withholding or withdrawing treatment pursuant to the Advance Directive. This certification must be redone no less than every 180 days so long as treatment is being administered pursuant to the Advance Directive.

F. ***Terminal Condition and Life-Prolonging Procedures***.

1. <u>Terminal Condition Required.</u> In order for an Advance Directive to authorize the "providing, withholding or withdrawal of life prolonging procedures", the patient must be found to be in a "terminal condition".

2. <u>Definition of Terminal Condition.</u> Virginia Code Annotated, § 54.1-2982.

"* * * a condition caused by injury, disease or illness from which to a reasonable degree of medical probability, a patient cannot recover and (i) the patient's death is imminent or (ii) the patient is in a persistent vegetative state."

G. ***The Need to Provide Comfort Care to Patient.***

1. The statute is clear in granting the physician the authority to administer medication to provide "comfort care" and to "alleviate pain".

2. The statutory advance directive states, "This authorization specifically includes the power to consent to the administration of dosages of pain-relieving medication in excess of standard dosages in an amount sufficient to relieve pain, even if such medication carries the risk of addiction or inadvertently hastens my death."

H. ***Must Consider Risks, Benefits, Beliefs, and Values.***

1. The substituted decision maker that is allowed to make the treatment decision must make a good faith effort prior to consenting to the treatment:

    a. To determine the risks, benefits of, and alternatives to the treatment.

    b. To determine the religious beliefs and basic values of the patient.

    c. To inform the patient to the extent possible of the proposed treatment and the fact that someone else is authorized to make a decision regarding such treatment.

2. The decision maker then must also take into consideration any preferences previously expressed by the patient regarding such treatment in so far as it might be known. If unknown, the decision maker must make the decision based on the patient's best interests.

J. ***Effectiveness of the Advance Directive Under State Law Other Than the State Law Where It Was Prepared.***

1. The General Assembly has addressed the problem of the legality of Advance Directives prepared pursuant to the law of a state other than Virginia. The law provides that an Advance Directive executed in another

state shall be deemed to be valid in Virginia, if the directive is drawn in compliance with Virginia law or the law of the state where executed.

2 Many states have enacted similar legislation to Virginia.

IX. SSI GUIDELINES

A. Countable Resources.

SSI recipient is allowed to have only $2,000 or less in non-protected resources. If resources exceed this during any calendar month the beneficiary's SSI benefits may be terminated. i.e. second car, savings account, cash surrender value of life insurance.

B. Non-Countable Resources.

Exempt assets are not counted in determining eligibility. May freely purchase these and give them to the beneficiary but do not give the beneficiary money to purchase exempt assets because payment of money is always considered income. Examples of excluded resources are: a home, household goods, one automobile needed for transportation or transportation of family members, medical treatments, etc, life insurance, if value less than $1,500, and all term policies, a burial plot. Other items included are personal effects such as books, games, travel television etc.

C. Guidelines.

Can give distributions which would not be considered income for SSI by making payments to a provider of medical or social services. Also, if you want to give the beneficiary what is call *in-kind* support and maintenance income, you should buy goods and give them directly to the beneficiary, make a direct payment to a provider (such as an appliance store) or use a voucher which should always be non-transferable and non-refundable i.e. buy the voucher with a credit card you hold. Can also pay for beneficiary to receive services. If you give the beneficiary an airline ticket, it <u>must</u> be non-refundable. Deeming occurs if child lives with ineligible parent, but stops applying the month following the child's 18th birthday.

D. ISM

If the beneficiary receives food or shelter as a result of payment, the beneficiary will have income in the form of "*in-kind support and maintenance*." If beneficiary receives ISM, his SSI benefits will be reduced because the SSI benefits are specifically intended to pay for a person's food, clothing and shelter and if that person receives those good or services from another source, less SSI benefits are needed. By paying rent, grocery bills or meals you are providing ISM and in theory reducing his need for SSI benefits.

In-kind support and maintenance is valued by the one-third-reduction rule, or the presumed-value rule, depending on the person's living arrangements. If a claimant is living in another person's household for a full calendar month and receives both food and shelter from that other person, the SSI benefit will be reduced by one third. The actual dollar value will not be calculated. The one-third reduction can be avoided if the claimant pays his pro rata share of household expenses. This would be calculated by dividing the average monthly household operating expenses by the number of people in the household, regardless of age.

E. The SSI benefit rate for 2011 is $674 for one person.

F. Do's and Don'ts – What should the parent of grandparent of a child or grandchild with special needs do:

- Make gifts to the child or grandchild with special needs in the form of a gift to an SNT
- Coordinate the planning for the child or grandchild with all family members.
- Use life insurance to fund an SNT for the benefit of the child or grandchild to create a sufficiently large asset base to meet the child's needs mot met by public benefits.
- Execute a durable power of attorney authorizing the agent to create or fund an SNT for the disabled child or grandchild