SPEAKER NOTES

Providing a Financial Future for Your Mentally Ill Relative

Summarized by Thomas T. Thomas

The future holds many uncertainties for families with a mentally ill relative, not the least of them financial. In addition to the questionable stability of Supplemental Security Income (SSI) and MediCal benefits, parents face the issue of how to provide for their children when they no longer can.

Janet Fairchild, the speaker at our July 25 meeting, is a local attorney who specializes in wills, revocable trusts, and special needs trusts. She is a graduate of Boalt Hall and teaches a course in estate planning at the Albany Adult School.

This is a very technical field, she stressed. Tax law and benefit regulations are continually changing as the government reacts to the development of new inheritance instruments. In consequence, few of the trust mechanisms she spoke about even existed fifteen or twenty years ago, so the attorney you deal with should be a specialist in this area.

Fairchild noted four issues to address in your estate planning:

- Taking care of your own health.
- Managing assets during your own lifetime.
- Conveying those assets to your heirs.
- Managing assets during the life of your disabled heir.

One of the best ways to deal with the first two issues, your own health and assets, is by executing a **durable power of attorney.** This lets you name any person—a spouse, child, or other party—to make decisions about your health and property if you no longer can. This document can be very useful because, when you are ill, you may not be able to visit the county clerk's or notary public's offices to conduct important business.

A **living will,** on the other hand, is the document you sign stating that you do not want to be left on life support after brain function is gone. Fairchild cautioned that this is an old idea, not always recognized by courts in the past, and so there are many variants floating around. None of them, in fact, is ever titled "a living will." Kaiser and other local hospitals will provide you with a California-approved document to sign, along with other releases.

The traditional method of inheritance, passing your goods on to your heirs, is through **a will.** In ancient Anglo-Saxon usage, a dying person called in two village elders and declared his or her "will" for the transfer of land and household goods; these witnesses then became responsible for enforcing the transfer. When church law came to dominate in this matter, the will was written down and enforced through an executor.

A newer way to transfer property is through **a trust.** In this case you deed your assets over to a trustee, who manages them for your beneficiary.

Today, the **revocable living trust** puts a slight twist on this principal because you become your own trustee and manage the assets yourself. The Internal Revenue Service does not view this as an actual transfer—which is good, meaning there are no taxes to pay—but the transaction is still recognized by law. In addition, you can have a subsequent trustee named to manage the assets when you die or can no longer manage for yourself.

This case presents some overlap with the durable power of attorney. Because the trustee is clear legal owner of the assets, title companies tend to accept trusts more readily than powers of attorney. However, the latter are gaining in acceptability, especially if the heirs are unlikely to contest the arrangement.

The primary reason for setting up a revocable living trust is that it avoids probate. That process alone can absorb a minimum 2 percent of the estate's value if you're leaving more than about $200,000.

Under present law there are no estate taxes on assets up to $600,000 (or $1.2 million in the case of a joint husband-wife estate). One way to avoid estate taxes is through a **planned giving program.** Over and above the $600,000 limit, you may give up to $10,000 per year to named persons before you die without tax consequences.

Another reason for establishing a living trust is to take care of a family member who can't manage for him- or herself, or whose own assets must remain below certain maximums to retain SSI/MediCal eligibility. In this case the best approach might be a **special needs trust (SNT),** which is often combined with a living trust.

SNTs are a new instrument, and currently state and federal regulations are in conflict over them, especially in the area of SSI eligibility. The state is concerned with people withholding assets that could otherwise provide for a disabled person's care. This is not a concern of the wealthy, who write trusts with abandon, but is a major concern for middle-class parents. After all, why pass along the money if it will simply disappear in replacing the SSI and Social Security coverages which already exist?

Right now, internal Social Security procedures do not count SNT assets toward eligibility if there is no provision for the beneficiary to gain access to the money. But some state regulations require that any excess in an SNT after the beneficiary's death must be turned over to SSI and MediCal to make up for past benefit payments.

However, all of these regulations are currently in flux, Fairchild warned. In figuring the costs of an SNT—which can be approximately four times those of a simple will, she said—you should add in the fees for ongoing legal advice as laws governing the trust change. It may also make sense to pay for a private professional conservator, who will charge $60 to $70 per hour (far less than an attorney or accountant) to administer the trust for you.

An alternative to private conservatorship is the **pooled income trust,** similar to the Proxy Parent Foundation run by AMI in California. Managing the investment strategy for a large pool of money and defending the arrangement against changing state regulation is a good way to reduce the cost for individual participants.

If the costs of an SNT are prohibitive, Fairchild said, then you can avoid them by using your assets to buy **exempt resources** for your disabled dependent. The largest and most obvious example is a place to live. Others might be an inexpensive auto, medical equipment, education, and other services.

Four categories of SNT are legal today in California:

1. Setting up an SNT as part of a parent's living trust or will, which is the most controllable and predictable arrangement. This type of SNT should be administered by a trustee other than the dependent's legal guardian, because courts tend to view guardians as likely to give the beneficiary too easy access to assets.
2. Joining a pooled income trust. This arrangement is exempt under federal law if the shares are administered separately (i.e., the assets are not divided equally among all parties) and if any excess in a share goes to the state upon the beneficiary's death.
3. Setting up a personal-injury SNT, which applies to cases involving catastrophic accident. The court simply transfers the jury award or settlement amount to the trustee.
4. Creating a living trust to manage the funds a disabled person receives from an inheritance. This is the poorest choice, Fairchild said, because it can void MediCal eligibility for three years.

There are several legal clauses you will want to include when having your attorney create an SNT.

First, there should be a clause prohibiting distributions that will interfere with SSI/MediCal eligibility. Instead, you may want to arrange for in-kind support and maintenance (ISM), involving items other than the rent, food, and clothing covered by SSI. Substitute distributions might cover education, travel, recreation, telephone and other utilities, gardening, or home-repair costs. To achieve this goal, the terms of the trust should leave the trustee as much flexibility as possible.

Alternatively, you can have the SNT make distributions which exceed the SSI's income limit of $165 per month—but schedule them for just twice a year. In this way, the SSI benefit is canceled only during those two months.

Second, the SNT should include a "self-destruct" clause which terminates the arrangement if changes in the law make the trust or its terms disadvantageous to your beneficiary. Continuing legal review and advice to the trustee are important features to provide for in this case.

There are many legal pitfalls to creating and implementing a special needs trust, Fairchild said. Still, when prepared by an attorney who specializes in estate planning and when administered by a conscientious trustee, an SNT can be the least expensive, least taxed way to provide adequately for the welfare of your disabled heir.