

Third-Party Special Needs Trusts: Peace of Mind for Caregivers

We are all aware of the importance of getting our family's financial and legal affairs in order. For family members of individuals with Alzheimer's disease, the importance of doing advance planning is magnified.

There are a lot of issues facing family members when a relative has Alzheimer's disease. One of the items that are most often overlooked is what happens if the caregiver dies before the family member with Alzheimer's disease. This is certainly understandable, given the tremendous emotional strains and other issues that must be confronted when a family member is ill. While there is no perfect replacement for a caregiver's love and care, some planning methods are better than others.

A Typical Situation

Consider this family's situation:

John and Sally have a modest estate: a home, some money in the bank and retirement accounts from when they were both working. They also have two adult children: Charlie and Emily. Emily is independent and doing well financially. Charlie, who is married, has been bouncing around from job to job and has never really found himself. Finan-

cially, he can't seem to hold onto money when it comes his way. Emily, who is not married, has given up her job to help as-

provided for him for the rest of his life; otherwise, he might have to go into a nursing home.



A third-party special needs trust may be the ideal arrangement for some families.

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care for John is very important to Emily and Sally. They understand that John is not able to live independently or support himself. He will need a home, income and a support system

Without appropriate estate planning, John will inherit from Sally or Emily in the event either of them dies before him. Since John is not able to manage financial assets, this would most likely require the court appointment of a guardian for John, unless John has executed advance directives such as a power of attorney appointing agents other than Sally or Emily. Such a guardian would have to manage John's assets and account to the court each year.

In addition, the assets that John receives may preclude him from obtaining certain types of governmental assistance benefits without the assets being spent down on the cost of his care. The area of governmental benefit programs is complex, as John may be entitled to one or more programs and the requirements are different for each type of program. For example, John may be on Medicaid and his inheritance would disqualify him from those benefits until the money is spent down since Medicaid is a means-tested program, which means there are strict asset and income requirements

that all Medicaid beneficiaries must comply with.

Based on this scenario, Emily and Sally are considering estate planning. They are thinking of leaving all their assets to the survivor of the two of them, or, to Charlie since he has promised to take care of John if anything happens to Emily and Sally.

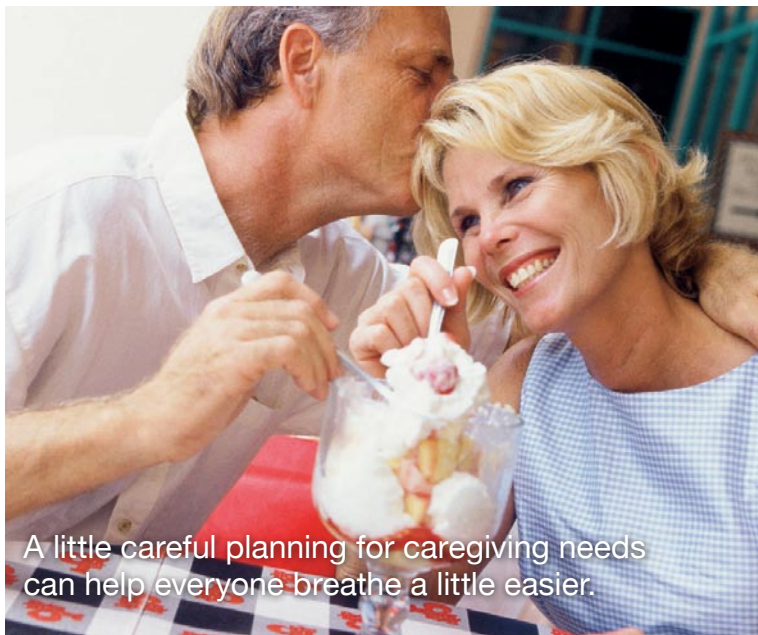
Is this a good solution?

A Better Approach

Actually, this solution has serious problems. No assets are legally protected for John and he may live for several years after his caregivers pass away. Moreover, although well-intentioned, Charlie may not live up to his commitment. This could happen should Charlie have financial problems, become ill himself, get divorced or die. John's security is imperiled.

A good solution is the creation of a third-party special needs trust (also known as a supplemental needs trust) for John. This trust, drafted specifically for this purpose, can be created as part of Emily or Sally's testamentary distribution plan when they die. A plan with such a trust does not rely on the moral commitments of others to be successful. The term "third-party" special needs trust (SNT) means that the assets used to fund the trust do not belong to John; they are assets of a "third-party." In this case the assets used to fund the trust may be assets of Emily and Sally. In many cases, caregivers such as Emily and Sally do not have sufficient assets to meet their relative's needs after they die since more formal arrangements with paid caregivers need to be made. One way of solving this problem is to create a third-party SNT and fund it with life insurance that will pay the life insurance proceeds to the SNT upon

the death of the caregiver. By setting up and funding a third-party special needs trust; the caregivers will ensure



A little careful planning for caregiving needs can help everyone breathe a little easier.

the highest quality of life for John.

Drafting a Successful SNT

The SNT would be designed to hold John's inheritance. It needs to be carefully drafted so that the assets in the trust can be used to enhance John's lifestyle and not cause him to lose his needs-based benefits. In most of these means-tested programs, the beneficiary's receipt of funds will terminate the beneficiary's participation in the program. SNTs are designed to allow the beneficiary to maintain eligibility for most means-tested programs, while still allowing the trustee to access trust funds to pay for goods and services that enhance the quality of the beneficiary's life. For example, the state Medicaid system may pay very little in the way of private duty nurses; however, the funds in the SNT can be used for this purpose. Also, the funds in the SNT can be used to take John on vacations or other quality-of-life excursions. Neither of these distributions will reduce John's needs-based benefits.

Since a portion of Sally's estate is held in individual retirement accounts

(IRAs), care must be taken regarding the timing and distribution of such funds to maximize tax savings. When an IRA beneficiary has medical needs such as John does, even more care must be taken to ensure that the tax benefits are maximized while maintaining access to much-needed government-financed health care programs.

Certain types of trusts require the beneficiary to take at least the required minimum distribution from the IRA each year and then pass that amount directly to the beneficiary. In general, this type of trust may make

sense from a tax perspective; however, trust assets paid out directly to the beneficiary will disqualify the beneficiary from participation in most means-tested programs. Other types of trusts allow the trustee to accumulate income (including the minimum distributions taken by the trustee) within the trust. While this type of trust may preserve government benefits, it may not be the most tax-efficient way to take distributions from the IRA, depending on your individual circumstances.

Of course, there is no one perfect solution that works just right for every family. However, it is important to remember that a plan be put in place to provide care for your relative with Alzheimer's disease in the event you pass away before your loved one. ■

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