

Insights for Preferred Clients



Estate planning: caring for family members with special needs

While estate planning is a challenge in the best of circumstances, the complexity of designing an effective estate plan increases significantly for families where one or more members have special needs. Typical estate planning goals, such as distributing wealth equally between children, must be reconsidered. A family also encounters additional government regulations that influence the amount and method for transferring assets to family members with disabilities.

There is no universal definition of “special needs”, but there are several defining conditions from an estate planning perspective. First, the person has a physical or mental disability that effectively prevents him or her from managing their own personal finances and legal affairs. This disability could be congenital, caused by illness or accident or the result of advanced age. Second, the person requires ongoing care in an institutional or group home or through private in-home care. The final condition is that the person qualifies for some form of government assistance, such as the Social Security Administration’s Supplemental Security Income (SSI) program or Medicaid health services.

Unique challenges

Traditional estate planning for wealthy families often focuses on maximizing the amount of assets transferred from the older generation to children and grandchildren. However, that strategy can produce unexpected negative consequences for family members with special needs. Avoiding these consequences requires an integration of the family’s estate plan, the special needs person’s financial requirements and government regulations. In particular, the estate plan should not jeopardize any governmental assistance the family member receives. “The goal is to earmark part of a family’s wealth for the special needs person in such a way that the person is not deprived of any governmental entitlements,” says James K. Treadwell, an estate planning attorney with Karr Tuttle Campbell in Seattle, Washington, and member of the UBS Attorney Network program,* with extensive experience helping special needs families.

Children

Eligibility for government benefits depends on the special needs person’s age and, for adults, financial resources. Children under age 18 can apply for Social Security disability benefits, special education resources and locally

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based resources. Disabled adults—age 18 and older—are eligible to receive a monthly income allowance from SSI, even if they continue to live at home with their parents. They can also receive health services through Medicaid.

Benefits for disabled adults have strict needs-based qualification rules, however. The value of the recipient's assets cannot exceed \$2,000 for a single person and \$3,000 for a couple (excluding a car, home and household possessions). In addition, if the disabled person earns more than \$20 a month of "countable income," which includes not only unearned income such as interest and dividends, but also cash gifts, the disabled person's SSI benefit will be reduced.

These financial qualification rules create a unique estate planning challenge. For example, many parents and grandparents regularly gift assets to younger generations. If the special needs family member is receiving government benefits and the gift increases his or her income or assets above the stipulated limits, these gifts (or an inheritance) can have serious consequences. The special needs family member immediately becomes ineligible for government benefits as long as they have more than \$2,000 in assets. He or she must now pay for his or her own medical care, including medicine, doctor's visits, physical therapy and personal care attendants. If the person lives in a group home, the person must now pay for the cost of residency and services. The person remains ineligible for government assistance until his or her income and assets again fall below the qualification limits. The person may also become ineligible for available benefits from state public assistance programs.

Structured settlements

Structured settlements can have a similar impact on a disabled person's eligibility for government benefits. These arrangements, which typically result from personal injury or medical malpractice cases, provide periodic payments over time instead of a lump-sum settlement. If the insurance company makes payment directly to the special needs family member, the government will count the amount paid against the qualification limits.

Spouses

Children aren't the only family members who may have special needs. Treadwell points out that spouses may also become disabled due to accidents or debilitating illnesses, such as Alzheimer's or dementia. In order to qualify for government benefits, disabled spouses must meet needs-based tests that impose limits on their income and assets.

The usual approach to qualifying a disabled spouse is to reduce his or her income and assets below the financial limits by transferring assets to the healthy spouse, though this may result in an ineligibility period. And for married couples with children from a previous marriage, this approach can be controversial with the disabled spouse's children. To illustrate, assume that both spouses have two children from their previous marriages and each spouse's estate plan provides for a bequest to their children from the previous marriage. (The bequest could be delivered immediately after the parent's death or after the surviving spouse's death.)

The husband is showing early signs of dementia. If he transfers his individually owned assets to his wife and gives her his share of jointly owned property,

there will be no assets in his estate for distribution to his children. In a sense, he has disinherited them unless his spouse promises to comply with his original bequests. A marital trust may address some of these issues.

Married couples in community property states face an additional challenge. (These states include Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington and Wisconsin.) These states regard property purchased during a marriage as community property and both spouses have an equal right to possess the property during their marriage. Removing assets from the disabled spouse's ownership requires that spouse to revoke the community property agreement.

Planning techniques

Each family's situation is unique, but in most cases there are several planning techniques worth considering, including:

A review of beneficiary designations. Several financial assets, such as retirement plans and life insurance policies, allow the owner to name a beneficiary or multiple beneficiaries who inherit the asset when the owner dies. Spouses, parents and grandparents should review their beneficiary designations to avoid inadvertently naming the special needs family member as a beneficiary.

Special needs trusts. A special needs trust holds property for the benefit of a disabled person. These trusts offer an important advantage over direct gifts or inheritances. Assuming the trust is structured properly, its assets do not belong to the beneficiary. (The trust's assets do not count against the \$2,000 limitation for programs such as SSI.) This arrangement allows the trust to provide

benefits to the family member without jeopardizing his or her eligibility for government benefits.

A special needs trust can supplement government benefits by providing for:

- Clothing
- Computer and electronic equipment
- Education
- Entertainment
- Eyeglasses
- Health checkups and supplemental medical and dental care
- A home health aide
- Insurance premiums
- Maintenance
- Rehabilitation
- Transportation (including vehicle purchase)
- Trips
- Athletic training and competitions such as the Special Olympics

Special needs trusts can hold a variety of assets, including cash, securities, personal property and real estate. The trust can also own and be the beneficiary of a life insurance policy. In addition, structured settlements can be paid to a trust instead of directly to the injured person, allowing the disabled person to retain eligibility for government programs.

The family members who establish the trust (the grantors) determine how the trust will be set up. In particular, they should address the following issues:

- *Selection of trustees.* Corporate trustees provide expertise in technical areas, such as investment management and tax reporting. Individual trustees, particularly non-donor family members, bring first-hand knowledge of the beneficiary. A special needs trust can have corporate and individuals as co-trustees, an arrangement that

combines technical expertise and personal involvement.

Letters of Intent. A letter of intent is not a legal document. Instead, it is a personal communication from the disabled person's primary caregiver to future caregivers. It allows the current caregiver to share insights about the special needs family member's likes and dislikes, personal preferences: "Robert likes cheese pizza on Friday nights. Don't buy him shirts with buttons." In a sense, the letter serves as a handbook for future caregivers.

Guardianships. A guardianship (or conservatorship) grants an adult legal power to make decisions for a disabled person who cannot make decisions for himself or herself. A court proceeding is required for a guardian to be appointed.

An example

The following hypothetical case illustrates one aspect of the estate planning process for a special needs family. The parents are both in their mid-sixties with a net worth of approximately \$8 million. They have three adult children, one of whom has Down syndrome. That child lives with her parents and receives benefits from several government programs, including subsidized medical care and employment.

The parents are concerned about two issues. The first issue concerns their own capacities as they age. They realize that, at some point, they will be unable to provide housing for their child. She will need some form of assisted living, such as a group home. The second issue concerns the risk that the parents die unexpectedly. How should their estate plan be designed in order to deal with this unique situation? If their estates

provide a direct distribution to their Down syndrome daughter, she will immediately lose her benefits eligibility.

In these circumstances, attorney Treadwell recommends that the parents establish and fund a special needs trust with an independent trustee for the Down syndrome child. "The trustee would invest the trust's assets appropriately to ensure that income and, if necessary, principal would be made available to that child. The trust distributions could provide for unexpected expenses, entertainment and other items in a fashion that won't disqualify the child of government entitlements," he says.

How much of their wealth should the parents bequeath to the special needs trust? Treadwell notes that it may not be necessary for them to leave a full one-third share because entitlement programs provide for the child's basic needs. He suggests that they might leave less than a one-third share—perhaps \$500,000 to \$1 million—to the special needs trust upon the death of the surviving spouse. "The balance of their estates would go to their other two children either directly or in trust," he says.

Finding a balance

Families with special needs members must balance their desire to help the disabled person financially with the recognition that unplanned assistance can harm more than it helps. The restrictions imposed on the disabled person's financial resources require other family members to consider nontraditional estate planning techniques. By using these techniques and adhering to the regulations, families with substantial wealth can create estate plans to help achieve the desired outcomes.

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