ESTATE PLANNING FOR DISABLED FAMILY MEMBERS: THIRD PARTY TRUST PLANNING[1]

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I. DEFINING THE ISSUE.

A. Our clients[2] come to us with concerns of how to provide for the long-term care of a Disabled Beneficiary (DB)[3] when they no longer can because of their own age or death. The core issues will likely be:

1. Protecting DB's eligibility to receive government Benefits,[4] which can be lost if the DB has excess "available"[5] income, assets or other resources.
2. Limiting any cost-of-care liability which can be asserted against the DB and possibly the family for the benefits received (generally paid out of any remaining assets after the death of the DB).
3. Dividing the assets a fair manner between family members.

B. Options for Making Distributions to a DB:

1. Disinherit the DB. Normally an option when Client has insufficient resources to establish a trust for the DB.[6]
2. Purchase of Exempt Assets.
3. Outright Distribution to DB. Not recommended unless the DB is capable of caring for himself and/or the funds will not adversely affect his Benefits.
4. The "Informal Trust."

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[2] This outline assumes that our "client" is one or both of the parents and not the DB. As always, it is important to address in writing who the client is and is not for conflict purposes.

[3] The "DB" is often the other spouse, a child, grandchild, sibling, parent, aunt, uncle, niece, nephew, etc., and may be either an adult or child suffering from different degrees of physical or mental disabilities which may or may not render the person fully or partially incompetent.

[4] "Benefits" as used in this outline, shall mean any means-tested benefit such as federal and/or state income or medical benefits paid under Social Security, Supplemental Security Income (SSI), Medicare and Medicaid for the care and benefit of the aged or disabled, with primary emphasis on need-based programs designed for the impoverished (SSI and Medicaid).

[5] See 20 CFR §416.1201 for the meaning of "available" for purposes of SSI and Medicaid eligibility.

[6] It is not recommended that one leave a disinherited beneficiary a nominal amount, *e.g.*, "I devise to Joey the sum of $10," given that this can create certain rights as a beneficiary that would not necessarily be available to a person who is truly disinherited as a beneficiary.

a. In conjunction to disinheriting the DB, the client might leave all the funds to a sibling or family friend with the expectation or moral obligation that the resources will be used to benefit the DB.

b. The obvious risk is that the funds will not be used as expected because of possible mismanagement, poor investments, self-use/benefit (*e.g.*, the trip to Las Vegas), creditor claims, divorce, death, etc.

c. Using the funds for the DB will likely create personal income, gift and/or estate tax issues for the sibling.

5. The "Formal Trust."

a. A written trust that will provide for <u>mandatory</u> distributions that will cover 100% of the cost of care for the life of the DB; or,

b. A written trust that will provide purely <u>discretionary</u> distributions for the supplemental care and/or the special non-support needs of the DB during his/her remaining life ("third-party trust" planning) while remaining eligible for applicable Benefits.

II. WHAT IS THIRD-PARTY TRUST PLANNING?

A. Third-party trust[7] planning involves the creation of inter vivos[8] or testamentary discretionary spendthrift trust by a person (the "settlor") for the benefit of another person (the "beneficiary") who is not the settlor, with assets not "owned" by the beneficiary.

1. In the context of a DB, normally a third-party trust will allow for the non-mandatory purely discretionary distributions for the supplemental care and needs (non-support) of the DB.

2. A pure third-party trust will be not be subject to the creditors of a DB in Alaska[9] and is not required to reimburse the state for Benefits expended on behalf of the DB.

B. In contrast to a third-party trust, a "self-settled trust" is any trust that is self-created by a settlor (or a court) with his own assets for the benefit of himself and possibly others.[10]

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[7] A "third-party trust," also known as a "supplemental needs trust," is generally created by a person other than the DB, and gives the trustee the unlimited discretionary authority to make distributions from the trust. In contrast, a "special needs trust" is created by the DB for himself.

[8] "Inter vivos" means a trust created during life by written agreement between the settlor and the trustee, as compared to a "testamentary" trust which is created at the time of death by a testamentary instrument such as a will of revocable living trust. The creation of an inter vivos trust will likely involve federal gift tax issues.

[9] See AS 34.40.110 and Restatement (Second) of Trusts §§155 and 156.

[10] Federal law allows for the creation of two types of self-settled special needs trusts that can be created with assets of an SSI or Medicaid recipient without losing eligibility for those benefits: (i) the Medicaid payback trust under 42 USC 1396p(d)(4)(A); and, (ii) the pooled trust account under 42 USC 1396p(d)(4)(C).

1. In the context of a DB, normally a self-settled trust will render the settlor ineligible for most means-tested public assistance programs and Benefits unless it qualifies as Medicaid payback trust under 42 USC 1396p(d)(4)(A).
2. A self-settled trust generally does not protect assets from the settlor-beneficiary's creditors.[11]

C. Applicable laws generally protect a third-party trust from creditor claims because:
1. The trust is funded with assets that do not belong to the DB.
2. The settlor has no legal obligation to support the DB beyond the age of minority or after death.
3. The assets are irrevocably set aside in trust and are distributed solely at the discretion of a trustee.
4. The settlor's intent is clearly stated in the governing trust instrument.

III. ESTATE PLANNING CONSIDERATIONS

A. Primary Focus:
1. Providing for the long-term supplemental assistance and care of the DB — What level of care is needed and for what reason?
2. The financial protection and well-being of the DB.
3. Designating guardians, conservators and trustees for the DB.
4. Naming a family member or friend who can serve as an independent "protector" or advocate with the ultimate power to designate new/additional fiduciaries over the DB.
5. Distributing assets "fairly" between other family members in a manner that balances the needs of the DB and other family members.
6. Providing a plan or structure to ensure that the funds left for the DB will be used in a manner that is consistent with the current and long-term goals of the client, DB, and family, all within the best interests of the DB.
7. Above all, avoiding unnecessary interference with the DB's continued eligibility for Benefits or liability for cost of care.

B. The Interview Process:
1. Understand the dynamics of the family. Understand the client's assets, liabilities and resources that are available to meet the needs of the DB and others.
2. How much should be left for the DB? How much is really needed?
3. Information needed about the DB:
   a. Actual and developmental age.
   b. Nature and severity of the mental and/or physical disabilities.
   c. Specific medical or treatment needs.
   d. Personality and behavioral traits.
   e. Current abilities and limitations (walk, talk, dress, public transportation, etc.).

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[11] See Restatement (3d) Trust §60. Alaska, along with a small number of other states, have enacted legislation to allow self-settled trusts to be protected from the settlor's own creditors if certain requirements are met and the transfer to the trust was not fraudulent. A self-settled Alaska Trust created by a DB will normally not provide the creditor protection sought given that such a transfer to a trust would likely be a fraudulent, unless such transfer was made at least five (5) years prior to the need for Benefits.

f. Education and/or vocational training.
g. Long-term prognosis and/or possible advances in treatment.
h. Future medical treatment expected (*e.g.*, “Joe will need another two surgeries before he is 18”).
i. The realistic life expectancy; is a doctor’s opinion needed?
j. Ability for self-care/support in the present and future.
k. Current living/housing arrangements.
l. Current available Benefits; consider impact of possible future changes.
m. Current private and public cost of care in today’s dollars; consider running an economic projection of possible future costs.
n. Assets or accounts “owned” by the DB.
o. Other financial provisions or trusts established by others for the DB (*e.g.*, grandparents, etc.)
p. The legal status of the relationship between Client and the DB – guardianship, conservatorship, etc.

C. Will vs. Revocable Living Trust:
1. Some form of dispositive testamentary instrument must be used to avoid the risk of the assets passing by intestate succession directly to the DB.
2. Consider using a last will and testament and not a revocable living trust.
a. 42 USC §1396p(d)(2)(A) provides that an individual shall be considered to have established a trust if assets of that individual were used to form all or part of a trust and if any of the following individuals established such a trust *other than by will* -
(1) the DB;
(2) the spouse of the DB;
(3) a person who has legal authority over the DB or the spouse of the DB;
(4) a person acting at the direction of the DB or spouse of the DB.
b. Therefore, as long as the settlor is not one of the prohibited persons listed above, then one can use either a last will and testament or revocable living trust. However, consider using only a will to avoid any confusion that the trust is “safe-harbored” under the statute.
3. Consider not using a revocable living trust given that any life time funding to the RLT will likely invoke the 5 year look back rule for purposes of disqualification.

D. Division of Assets:
1. How should the family assets be divided fairly?
2. What are the client’s goals for the funds? What level of care is expected or required?
3. How much does the DB really need? That will depend on the level of care the DB needs now and in the future.

E. Naming the Fiduciary(-ies):

1. Decisions need to be made as to who will be the primary and successor personal representative, trustee, guardian, conservator, legal advocate, health care agent, and/or the "protector."
2. Trustee:
    a. Normal considerations apply when naming a trustee and successor trustee(s) who will be responsible for investments, asset management, and making discretionary distributions.
    b. Consider: age, financial expertise, management skills, time available, desire to be involved and level of interest, ability to understand how trust distributions may affect the DB's Benefits.
    c. Non-corporate trustee, *e.g.*, a family member:
        (1) May provide a personal relationship and have specific knowledge of the unique needs of the DB.
        (2) May provide better monitoring of the day-to-day needs of the DB.
        (3) May better serve as a personal advocate for the DB when needed.
        (4) May likely serve without compensation.
        (5) May not have the necessary fiduciary or investment expertise needed resulting in an actual or apparent misuse of funds.
        (6) May create a conflict of interest if the trustee is also a remainder beneficiary.
        (7) Does the person have the capability and/or desire to serve?
        (8) Consider adding a provision waiving any conflicts between the DB and the sibling-trustee.
        (9) See discussion below re: Powers of Appointment
    d. Corporate Trustee:
        (1) Will provide professional fiduciary services, investment and asset management, and accounting functions.[12]
        (2) May be insensitive and not have a personal relationship with the DB, not taking the time or effort to fully understand the unique real needs of the DB.
        (3) Will charge a fee for services rendered.
        (4) The amount placed in trust may not be large enough to justify a commercial trustee or a minimum amount is required (*e.g.*, $500,000 minimum principal balance).
        (5) Is there a local office and specific trust officer?
    e. Co-Trustees:
        (1) It may be appropriate to name co-trustees – administration trustee, investment trustee, distribution trustee.
        (2) Consider splitting the duties between a corporate trustee (investments, management, accounting) and an individual trustee (distributions and advocate). Where there is a split of duties, it is important to carefully define the scope of the

[12] Some commercial trust companies have specific departments dedicated to management of special need trusts. The client should be encouraged to meet with managers of the trust departments to determine the level of comfort and expertise. Despite the cost, engaging the services of a commercial trust company can be liberating to the other family members.

authority of each and to seek the pre-approval of the commercial trustee regarding the terms of the appointment.

(3) In the alternative, designate in the document a person who is authorized to interface with the trustee on behalf of the DB and specifically directing the trustee to take into consideration the directions provided by the person named.

f. Name an adequate number of successor trustees.

g. Conflicts of Interest: Often a sibling is named as the trustee over the trust for the DB and this can create a conflict over distributions when there is either a sprinkle provision or the remainder is to pass in whole or in part to the trustee-beneficiary. It is appropriate to add a specific waiver of conflict so that the settlor's intent is very clear that the sibling can and should serve as trustee irrespective of any actual or apparent conflict.

3. Guardian/Conservator:[13]

a. A parent may make a testamentary appointment of a guardian for a minor or incapacitated adult.[14]

b. The real issue is who should serve as the guardian of the minor or adult DB after the death of the primary parent-guardian, and to what degree should the that guardian serve, *i.e.*, as a "full guardian" or "partial guardian".[15]

c. The client needs to understand that formal guardianship will add a level of complexity for the guardian given the court's supervision and possibly an unwanted stigma to the DB and/or restrictions of legal rights.

d. Consider:

(1) The client should seek the permission of the person named to be the guardian and review the requirements of such responsibilities.

(2) Should a bond be required or waived? If a bond is required, will the designated guardian/conservator want or be able to post a bond?

(3) Consider expressing a testamentary statement of intent requesting a full or partial guardianship, and/or any limitations that are appropriate to meet the developmental

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[13] AS 13.26.150(c)(6) provides that a court appointed full guardian has both the authority of a guardian (over the ward's person) and the authority of a conservator (over the ward's assets).

[14] AS 13.26.030 and 13.26.095; the appointment is generally effective when an acceptance is filed. AS 13.26.040 provides that a person over 14 may object to the appointment. Normally, a parent is the natural guardian of a minor until the child attains the age of majority (18), when there is a presumption that the adult-child is legally competent. After the age of majority, a formal guardianship proceeding will need to be implemented for a DB.

[15] AS 13.26.005(6) and 13.26.150(b).

needs of the DB, provided that such are not too restrictive to prevent changed circumstances.[16]

(4) Should the guardian also be the conservator, or should conservator-type duties be specifically delegated to the trustee or other third-party?

4. Legal Advocate:
   a. Normally the full guardian would be the legal advocate for the DB.[17] However, in some cases, the interests of the guardian and the DB-ward might be in conflict.
   b. Consider making a testamentary nomination of a specific person who will represent the DB and understand any unique family issues and goals. Although not necessarily legally binding, it may minimize the risk that the court names an unrelated independent third-party as the guardian *ad litem* who might be adverse to the family.
5. Health Care Agent:
   a. Normally the guardian has full authority to deal with health issues.
   b. It might be appropriate to name a person other than the guardian to have a health-care or medical power of attorney over the DB.
   c. It might be appropriate to provide in the testamentary instrument a request for appointment of a "partial guardian" setting forth the different duties and responsibilities of each "partial guardian," *i.e.*, one guardian is responsible of the day-to-day care giving of the DB, but the other partial guardian is responsible for all health care decisions of the DB.
6. The "Protector":
   a. Much like a "trust protector," consider appointing a beneficiary protector or advisor, a person who has the authority to challenge the guardian, trustee, etc. in the best interests of the DB, including the authority to terminate any fiduciary.
   b. It would be necessary to set forth in the testamentary instrument carefully the settlor's goals and intent for the "protector" and the scope of the protector's authority.
   c. Such a provision might be more appropriate when there are independent unrelated fiduciaries involved in the care of the DB and management of assets.

F. Gift Planning:
1. Generally:
   a. Normally, estate planning will utilize the donor's annual gift tax exclusions through a regular pattern of annual gifting.

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[16] It is important to carefully draft the pleadings with the appropriate restrictions. In one case the attorney requested, and the court granted, a "full guardianship and partial conservatorship" when the ward was only partially incapacitated. This lead to constant confusion for all parties involved.

[17] AS 13.26.150(c)(4).

b. The annual gift tax exclusion permits the transfer of a specified amount ($12,000 in 2007) to an unlimited number of donees,[18] or a single lifetime gift of $1,000,000.[19]

c. Gifts can be made to a UTMA account[20] or to an *inter vivos* trust.

d. One should also consider gift-splitting with the donor's spouse.[21]

2. Making unrestricted outright gifts to a DB will adversely affect Benefits. Therefore, gifts to a DB must be made in trust.

3. Because a gift to an *inter vivos* trust is considered a gift of a future interest, the gift will not qualify for the annual gift tax exclusion. To make the gift qualify for the annual gift tax exclusion as a present gift, the trust must be drafted to allow for use of *Crummey* withdrawals;[22] however, it is not appropriate to give a DB a *Crummey* power (see following discussion regarding *Crummey* powers).

4. It is important to remind other family members not to make gifts (or bequests) to a DB in an unrestricted form.

G. Life Insurance Planning:

1. Life insurance can be a useful tool to fund a testamentary third-party trust for the benefit of a DB.

2. In all cases, the life insurance should not be paid directly to the DB.

3. Review all life insurance policies with the Client.[23]

a. Is there adequate insurance? Is more needed?

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[18] See §2503(b); Rev. Proc. 2006-53, 2006-48 I.R.B. __, §3.32(1).

[19] The lifetime exemption is $1,000,000 and is no longer unified with the federal estate tax applicable credit amount (IRC §2505).

[20] A transfer to a UTMA account may be made during life or on death by testamentary instrument. AS 13.46.195(e) provides that an Alaska UTMA account may be designated to terminate at any time between the ages of 18 and 25, and by default terminates at 18. A gift to a DB in the form of UTMA is not recommended given that the asset will be considered an available resource when the UTMA account terminates at the designated age.

[21] With the consent of the donor's spouse, and if the spouse has not made independent gifts to the same DB, a gift made solely by one spouse may be deemed gifted by the donor's spouse as well, effectively doubling the annual exclusion gifts available. These so-called "split" gifts will permit the accumulation of value to occur outside the estate of the donor, presumably in the hands of a member of a younger generation than the donor. IRC §2513. Gift-splitting is used only when the donor's spouse does not want to gift her own assets to the donee, typically seen in a second marriage.

[22] See §2503(b) and (c). A *Crummey* right of withdrawal will generally allow a beneficiary the unrestricted present right to withdraw contribution to a trust for a specified period of time, *e.g.*, 35 days, thus making the gift a present interest gift and not future interest gift. The use of a properly drafted *Crummey* withdrawal power is beyond the scope of this material. *See also Crummy v. Comr*. 397 F.2d. 82 (9th Cir. 1968).

[23] Working with a qualified life insurance agent from a reputable company can be an invaluable tool and resource for the Client given the many different types of life insurance available.

b. Review ownership issues and whether the policy should held in an irrevocable life insurance trust for the benefit of DB and others.

c. Who is the beneficiary of each policy?

(1) Review actual designation of beneficiary forms – do not rely on the representations of the Client.

(2) Never name the DB as the primary or contingent beneficiary of a life insurance policy.

(3) Do not forget to consider designated beneficiaries of other insurance provided by the employer, union benefits, travel or credit cards.

d. Types of life insurance, term or whole life, and the different blends.

H. Retirement Account Planning:[24]

1. Planning In General.

a. A retirement account[25] can be left to a beneficiary either outright or in trust.

(1) If the funds are paid outright to the beneficiary, the beneficiary can elect to take the distribution outright (subject to immediate income tax), or through an inherited IRA which will allow the distributions to be paid as an annuity over his remaining life expectancy[26] (subject to income tax on each annuity payment received). In cases not involving a DB, this is by far the simplest solution.

(2) If the funds are paid to a trust, there will be different distribution results depending on the type and structure of the trust (*e.g.*, a "conduit trust," "non-see-through-accumulation trust," or "see-through accumulation trust").

b. As a general rule, it is better to leave money in a retirement account for as long as possible because of the income tax-deferred compounded growth of the funds.

(1) Economically, the longer assets stay in an income tax-deferred account, the faster the account will grow because of the compounded growth of the unpaid-deferred income taxes.

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[24] Most of this material was taken in whole or in part from N. Choate, *Life and Death Planning for Retirement Benefits* (6th ed., 2006).

[25] This refers to any type of retirement plan such as a defined contribution plan (401k, 403b) or IRA, all of which are subject to the minimum distribution rules (MRD). However, most of this discussion will apply only to IRA's given that the other types of plans are also governed by specific employer sponsored plan documents and define the methods of payout on the death of a participant – usually an annuity or rollover for surviving spouse, and outright to other beneficiaries with no annuity option to minimize the employer's ease of future administration after the death of an employee participant. Consequently, it is even more important to carefully plan for qualified retirement plan assets that might pass to a DB.

[26] The annuity payout will be based on the "minimum required distribution" (MRD) rules and will depend on whether the owner-participant died before or after his required beginning date (RBD).

(2) Therefore, if a long-term goal is to maximize compounded growth and investment returns after the death of the participant, then it is better to leave pre-taxed retirement money in the retirement account for as long as possible.

2. For a DB, there are two types of trusts that should be considered when it is important to leave retirement plan assets to the DB in trust:[27]

a. "See-through" Accumulation Trust:[28]

(1) If it is important to *require* distributions in the form of a life-expectancy payout annuity, then use a "see through" accumulation trust which will allow the retirement account benefits to be distributed to the trust as an annuity over the life expectancy of the oldest living remainder trust beneficiary.

(2) Given that a typical supplemental needs trust will normally allow for the purely discretionary distributions of income and/or principal to a DB, it is very important to provide in the trust document that the trustee should exercise caution and not distribute trust "income" to the DB unless the distributable net income (DNI) is less than the monthly amount ($1,656) allowed to retain all Benefits.[29]

b. "Non-see-through" Accumulation Trust: If retirement plan assets are the only available resource to leave to a DB, consider using a a "non-see-through" accumulation trust.

(1) In this case, the retirement plan is distributed directly to a third-party discretionary spend-thrift trust that does not qualify for the life-expectancy payout annuity method under the MRD rules (*i.e.*, "see-through" treatment), and therefore does not provide the economic benefit of income tax-deferred compounded growth.

(2) This type of trust works well when:

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[27] For an exhaustive review, *see* N. Choate, *Life and Death Planning for Retirement Benefits* (6th edition, 2006), and specifically ¶ 6.3.11 "Planning Choices: Trust for Disabled Beneficiary."

[28] *Id.*, at ¶ 6.3.06, wherein Ms. Choate refers to this type of trust as an "Accumulation trust: O/R-2-NLP (outright-to-now-living-persons trust)" and it is based on PLR 2004-38044, 2005-22012 and 2006-10026, which provides for one primary beneficiary, and one or more then living residual beneficiaries. With an O/R-2-NLP trust, the MRD is based on the life expectancy of the oldest living <u>remainder</u> beneficiary. Given that this type of trust has been blessed by the IRS only in private letter rulings, there is some risk that the IRS might either revoke or reinterpret its rulings in the future. Note: A charity cannot be a remainder beneficiary in this type of trust because it is not an "individual."

[29] Limiting the amount of income that the trustee can distribute to a DB creates an inherent economic conflict between the trust income tax rates and tax-deferred compounded growth of the retirement funds. Any income that is not distributed annually by the trust to the DB will be income taxed at highest income tax bracket. For 2006, a trust will pay a 35% income tax on income in excess of $10,050, whereas an individual will pay 35% income tax on income in excess of $336,550. Therefore, good fiduciary trust practice would normally maximize the distributable net income (DNI) to a beneficiary to minimize the income tax cost, but the distribution to a DB of more than $1,656 of income per month will adversely impact benefits, unless the excess is paid to a Miller Trust.

(a) There is no goal for the income tax-deferred compounded growth of the retirement assets (the accumulated funds will still grow, just not income tax-deferred);

(b) Funds are to be accumulated, reinvested and then distributed at the sole discretion of the trustee; and,

(c) Maximum flexibility in trust drafting is needed, *i.e.*, the creation of a third-party trust is needed to protect the resources for the special needs of the DB.

(3) The cost to this type of trust is the payment of all income taxes up front upon the funding of the trust at the *highest income tax rates*, the trust being funded with net after tax dollars.

3. Surviving Spouse as the DB:

a. If the surviving spouse is the DB,[30] then it is generally recommended not to leave retirement plan assets outright or in trust for the benefit of the DB-spouse. If such assets must be left to the DB-spouse, then all of the above points should be carefully considered before leaving retirement account assets to the surviving spouse.

b. If it is not important to qualify the retirement plan assets for the unlimited marital deduction, then use a normal credit shelter trust and draft it either as a "see-through" accumulation trust or as a "non-see-through" accumulation trust depending on the analysis above regarding the use of trusts.

c. If it is important to qualify the retirement plan assets for the unlimited marital deduction, careful planning and drafting is required, which is beyond the scope of this outline.[31]

(1) An outright distribution of retirement benefits that are rolled over into a spousal rollover IRA, will normally qualify for the unlimited marital deduction; however, a spousal rollover IRA will be counted as an available resource for determining available Benefits.

(2) Only two types of trusts qualify for a the unlimited marital deduction and both require that 100% of the income be distributed to the surviving spouse during his/her life.[32]

4. Retirement Account Caveats!

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[30] If the surviving spouse is not the DB, then normally the best planning is to name the surviving spouse as the primary beneficiary of the retirement account assets so that he/she can roll the account over into a spousal IRA, and in the alternative, use a normal see-through accumulation trust that is either a CST or QTIP trust. *See:* N. Choate, ¶ 6.3.14, "Practical Options: Trust for Spouse," which is written in the context of the surviving spouse not being the DB.

[31] *Id.*, ¶ 3.3 "Qualifying for the Marital Deduction."

[32] *See*: IRC §§ 2056(b)(5) and 2056(b)(7)(B)(ii). In almost all cases, a qualifying marital deduction trust should not be used for a DB-spouse given the mandatory distribution of income would cause loss of Benefits unless the excess income is distributed to a Miller Trust.

a. A normal "conduit" trust[33] or a "accumulation 100% grantor" trust[34] should not be used for a DB given that all of the income will taxed to the DB and will be counted as an available resource for determining available Benefits.

b. A charitable remainder trust (CRT) should not be used for the DB given that a CRT is required to make either annuity or unitrust distributions to the beneficiary which will be counted as an available resource for determining available Benefits.

5. Summary/Conclusions regarding Retirement Plan Assets:

a. If possible, avoid leaving retirement plan assets to a DB because distributions from the retirement plan will be treated as income to the DB and will be counted as an available resource for determining available Benefits.

b. If retirement plan assets must be left to a DB, consider using a "non-see-through" accumulation trust given the flexibility and despite the up front income tax cost.

I. Planning for a DB-Spouse:

1. Who do you represent for purposes of the conflict of interest? If the non-DB-spouse, then the DB-spouse must have his/her own counsel to avoid any conflicts. Where appropriate, it is important involve all family members in the planning.
2. Do not leave assets outright to the DB-souse given that such will be counted as an available resource for determining Benefits.
3. Consider transferring all assets to the non-DB-spouse. Although this will not provide much benefit during the joint lives, on death of the non-DB-spouse, all of the assets can pass into trust(s) for the benefit of the DB-spouse.
4. Consider executing a post-nuptial agreement waiving the statutory elective share (make sure there is adequate consideration for the waiver).
5. Use a last will and testament and not a revocable living trust.
6. Create a testamentary bypass-credit shelter trust in the form of a third-party trust (see below), and maximize funding on death of the non-DB-spouse using the non-DB-spouse's remaining applicable credit amount.[35] Have the client identify which assets might be the best to hold in the credit shelter trust.
7. Do not use a disclaimer to allow the DB-spouse to fund the credit shelter trust. Although effective for federal transfer tax rules, a qualified disclaimer will likely be counted as a resource to the DB-spouse.

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[33] A "conduit trust" is any trust where the trustee is required by the trust to distribute to the individual trust beneficiary all distributions the trustee receives from the retirement plan. The benefit of a conduit trust is that the beneficiary is forced to take distributions over his life expectancy. *See*: N. Choate, at ¶ 6.3.07.

[34] A trust where the trustee is authorized to accumulate within the trust distributions from the retirement plan and the beneficiary is treated as the "grantor" under the grantor trust rules of IRC §§ 671-678. *See*: *Id.*, at ¶ 6.3.08.

[35] Under current law, the federal applicable credit amount is $2,000,000 in 2007 and 2008, and $3,500,000 in 2009.

8. Consider creating a testamentary marital deduction trust.[36]
   a. Although a qualifying marital deduction trust will generally not meet the needs of a DB-spouse given that such trusts require a mandatory distribution of all income (which will be counted as an available resource for determining Benefits), excess income can be paid into a Miller Trust, subject to the right of reimbursement on death of the DB-spouse.
   b. Caveat! Make sure all family members understand that a marital deduction trust requires mandatory distribution of 100% of income and may be subject to federal estate taxes on death.
9. Consider funding the credit shelter trust in excess of the applicable credit amount at the cost of paying additional federal estate taxes on the death of the non-DB-spouse. Although unlikely, the economic cost of the estate tax (45%) might be less than the alternative of funding a QTIP and paying excess income to a Miller Trust and the right of reimbursement from the Miller Trust on the death of the DB-spouse.
10. In any trust created for the benefit of the DB-spouse:
   a. Do not give the DB-spouse a $5,000-5% withdrawal over trust principal given that such "power" can be used to force a distribution for the benefit of the DB-spouse, and thus affecting benefits.[37]
   b. Do not make the trust subject to ascertainable standards of "health, education, maintenance and support" given that support is an ascertainable standard and a court could force a distribution for support purposes.
11. Who should be Trustee of the trust for DB-spouse?
   a. The DB-spouse should not be the trustee.
   b. The non-DB-spouse should not serve as the trustee given his authority over the trust can be imputed to or for the benefit of the DB-spouse.
   c. Should a child-remainder beneficiary serve as trustee?
      (1) That is very typical.
      (2) However, see discussion below re: Powers of Appointment.

J. Parent's Letter of Instruction and Intent:
1. Given the history a parent has with the DB, it is appropriate to leave a detailed and up-to-date letter of instruction regarding the DB.
2. The letter might address the following issues:
   a. Personal history and general character of the DB.
   b. Medical history, needs, records, treatments, prognosis.
   c. General living needs, current and long-term.
   d. Services and Benefits available.
   e. Annual costs associated with care (direct out of pocket vs. government).

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[36] *See*: IRC §§ 2056(b)(5), 2056(b)(7) and/or 2056A.

[37] Under normal circumstances, the "five and five power" (the greater of $5,000 or 5% of principal) can be a useful estate planning tool since its availability will not cause the entire trust principal to be included in the holder's gross estate.

f. Education and vocational goals.
g. Housing-living expectations.
h. Service and care providers.
i. Names of individuals with personal knowledge of the DB and whom might be consulted.
j. Concerns over care, management, etc.
k. Expected mandatory vs. discretionary care duties.

IV. DRAFTING A TESTAMENTARY SUPPLEMENTAL THIRD-PARTY TRUST.

A. In General:

1. The key is to draft the trust so that the assets held by the trust will not be treated as countable resources of the DB, *i.e.*, that the DB cannot compel a distribution for support.
2. Federal Medicaid and SSI law, which is binding on the states, assures that person not responsible for the support of a DB may provide a source of funds to be used to enhance the quality of life of the DB, and federal law restrains states from treating as resources trusts from which the DB cannot compel distributions for support.[38]

B. Statement of Intent and Purpose:

1. A fundamental principal of trust law is that a settlor may dispose of his property in any manner desired, other than dispositions prohibited by law or contrary to public policy.
2. A statement should be included in the trust stating the settlor's strong intent that the trust is a wholly discretionary trust designed supplement government provided benefits, and that is not to provide support or supplant those Benefits.[39]
3. A strong precatory statement of intent and purpose might possibly provide:
   a. State that the settlor has no obligation of support, and, but for this trust, the settlor might have disinherited the DB.
   b. Affirmatively disavow any obligation by the trust to provide support for the DB, stating clearly that the sole purpose of the trust is "supplement, not supplant" public benefits.

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[38] See 42 USC 1396a; 20 CFR §416.1201(a)(1) and (c)(3); Program Operations Manual System (POMS) SI 01120.200(D)(1)(a).

[39] For example: "My son John is disabled and will likely rely on public benefit programs for much of his life. I will not always be there to help him and oversee is care. I know that he will have long-term supplemental and special requirements, including a need for advocacy, which will not be provided by publically funded programs. Therefore, it is my desire, but not my direction, that the Trustee of this trust, in the exercise of the Trustee's sole, absolute and uncontrolled discretion, provide supplemental goods and services for the benefit of John which will provide him dignity and grace, enhance his day to day care existence, and allow him the highest possible development of his abilities, but in a manner that will not supplant or jeopardize benefits he may receive from any public assistance programs. This paragraph shall be construed as being a precatory statement of my intent in creating this trust, and not as providing standards to guide the trustee in exercising its discretion to make distributions to or for the benefit of John."

c. The trust is established for the explicit and sole purpose of ensuring that the DB receives the resources and assistance needed to maximize his potential and to enjoy the best possible quality of life.

d. The trust shall not be eroded by the cost of medical or support care so long as such care can be provided with either the DB's own earnings (assets) and/or private and public financial assistance.

e. The trust is intended to supplement, not replace, the DB's earnings, if any, and available private and public benefits.

f. The trust is intended to benefit the DB during his life, including in ways not presently anticipated.

g. The trust is primarily, but not exclusively, for the benefit of the DB rather than the remainder beneficiaries.[40]

h. The trust is to protect the rights of the DB, and thus funds can be expended to help family members ensure the rights of the DB, either through their travel or other assistance.

i. The trust is to provide to the DB (and accompanying guardians) adequate recreational opportunities, travel and vacations.

C. Distributions of Income and Principal:

1. As a general rule, a trust that requires mandatory distributions will be counted as an available resource, whereas purely discretionary distributions will not. The distinction often turns on the intent of the settlor and whether the DB and/or others can force a distribution from the trust.

2. A third-party trust should prohibit any mandatory distributions of income or principal.

3. A third-party trust should expressly provide that no distributions can be made for the "support"[41] of the beneficiary. For example:

> No part of the income or principal of this trust may be distributed for the support of the Beneficiary such as for food, shelter or to replace any public assistance benefits for the which the beneficiary may be eligible through any state, federal or other governmental agency.

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[40] Care should be taken to avoid stating too strongly that the intent is to solely benefit the DB because a court might conclude that the trust is for the sole benefit and support of the DB, thus allowing the trust to be invaded by creditors. Therefore, in some cases, it might be appropriate to state an intent that any remaining assets are specifically intended to also benefit the remainder beneficiaries as part of the settlor's overall dispositive intent and estate planning goals.

[41] "Support" normally includes living expenses, medical care, care, comfort, maintenance, health, welfare, general well-being, or a combination thereof.

4. All distributions of principal and income should only be made at the sole and absolute discretion of the trustee. Define the meaning of "sole and absolute discretion."[42]
5. The trustee should have the express authority to accumulate income and all distributions of income and principal should be purely in the sole and absolute discretion of the trustee.
6. A third-party trust for a DB should not include a typical ascertainable standard such as "health, education, maintenance and support" given that such creates a "support" trust subject to the claims of creditors and will impact benefits.[43]

D. Choice of Law and Spendthrift Provisions:
1. It is very important in every trust to include a strong spendthrift provision that prohibits the alienation of any rights and complies with AS 34.40.110.
2. Consistent with the above, the trust should provide that it is to be governed solely by the laws of Alaska. Consider making the trust comply with AS 13.36.035(c).[44]

E. Limitation of Expenditures:
1. Consider limiting or prohibiting the trustee from using trust assets to cover basic support needs, basic medical care, and/or to reimburse the government for such cost of care, or from making distributions that might disqualify the DB from receiving benefits.
2. In the alternative, give the trustee the discretion to make disqualifying distributions if determined to be in the best interest of the DB. For example:

> I ask the Trustee to make reasonable efforts to avoid making distributions that supplant services, benefits or medical care otherwise available to the Beneficiary from governmental or

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[42] For example: "'Sole and Absolute' discretion shall mean that my Trustee shall have the complete, conclusive, full and final authority to make decisions over the subject matter so authorized, without review by any beneficiary, third-party or authority (administrative or judicial), provided however, judicial authority may review such decision only if it is first established that the Trustee was incapable of exercising such discretion as a result of being mentally incapacitated. Therefore, it is the intent to construe "sole and absolute" broadly and liberally in favor of the Trustee and if there is any judicial review of such discretion, it is the intent that the court not consider or evaluate whether the exercise of such discretion was reasonable, abused or a breach of any fiduciary standard, or how such decision impacted the beneficiary."

[43] Normally an ascertainable standard clause is included in a trust to prevent the trust estate from being included in the taxable estate of a trustee who is also a current or remainder beneficiary of the trust as a general poser of appointment (See discussion following re: Powers of Appointment). Therefore, if the trustee is also a beneficiary of the trust, it is appropriate to consider limiting distributions only to the DB during his life, specifically excluding any benefit to the remainder beneficiaries until after the death of the DB. A trust that provides for the "discretionary distributions for support" might work, but there is the risk that the trust will be counted as a resources.

[44] AS 13.36.036(c) provides, in general, that a trust will be governed conclusively by the laws of Alaska if the trust (i) has assets on deposit in Alaska; (ii) the trustee is a "qualified person" [see: 13.36.390(2)]; and (iii) some administration of the trust occurs in Alaska.

private sources, or both, unless the Trustee has determined, in his sole and absolute discretion, that the benefit to the Beneficiary from the particular trust distribution outweighs the reduction in a particular public benefit program that may be a consequence of the trust distribution.

3. Authorize the trustee to explore other need-based support options for the DB and to hire the necessary professionals to assist in that search or qualification procedure.
4. Consider requiring that before distributions can be made, the trustee must require or take into consideration other resources and earning potential or income the DB might have that he/she can use to help supplement the cost of care.

F. Accumulation of Income: Consider authorizing or requiring that all net income shall be accumulated and added to principal to make it even clearer that income is not available to the DB. Not distributing the annual DNI will increase the income taxes paid given the trust's marginal rate is higher than an individuals; however, this may be an acceptable economic cost of this type of trust and the goals of the settlor.

G. Expenditures for Other Needs:
1. The trust should be specifically set forth an intent for the type of expenditures that are contemplated to meet the supplemental needs of the DB.
2. It is appropriate to list items that might be needed:
   a. Upgrading or remodeling the DB living conditions, such as lifts, ramps, heated driveway, etc.
   b. Purchase of entertainment equipment, such as a TV, CD, stereo, DVD-player, computers, game boxes, etc.
   c. Payments for travel, including vacations, attending sporting events, medical care/treatment, camping, etc., and the cost of any travel assistant.
   d. Daily transportation, private carrier or upgraded accessible van.
   e. Reimbursing the reasonable cost of family to visit the DB.
   f. Purchase of gifts for relatives and friends.
3. Consider a provision that specifically authorizes family members of the DB to travel with the DB, to use assets (the vehicle), or to reside in real property (with or without the payment of rent) owned by the trust.

H. Periodic Evaluation and Visits:
1. Either require annual reviews or authorize discretionary periodic reviews to be paid for by the trust for an evaluation of the DB's current physical and mental conditions, progress or opportunities in the areas of education, work, training or rehabilitation, recreational and social needs, residential living conditions and available state and federal benefits.
2. The trust should either require trustee or authorize the payment of others to make frequent and unscheduled visits to evaluate the care and living conditions of the DB.

3. There should be a specific authorization to allow the trustee or agent to interview care providers, staff and review records related to the medical, education and living conditions.
4. The authorization should incorporate some HIPPA-type waiver or authorization, and if access is denied, the trustee should be authorized to seek court intervention and seek reimbursement from the care provider for such action.

I. Distributions to Other Beneficiaries:
1. Consider adding a “sprinkle” provision authorizing the trustee to make discretionary distributions not only to the DB but also to other family members during the life of the DB.
2. A sprinkle provision may further insulate the trust from the creditors of the DB given that the trust was intended to benefit not only the DB, but also remainder beneficiaries.
3. Care should be exercised if a beneficiary is also a trustee:
   a. Conflicts can arise over distributions between the supplemental needs of the DB and the discretionary needs of the other beneficiaries.
   b. Given that a third party trust should not have an ascertainable standard, there is the risk that the trustee-beneficiary will be deemed to have a general power of appointment. Therefore, consider providing that the authority to “sprinkle distributions” to a non-DB should be limited to an ascertainable standard to prevent the creation of a general power of appointment in care of the trustee-beneficiary.
   c. See discussion below re: Power of Appointments.

J. Manner of Distributions: Authorize the trustee to make direct distributions to and on behalf of the DB, including:
1. To the guardians (and others) to assist in the care and expenses of the guardianship, and authorize the trustee to require receipts or some budget plan for the expenditures.
2. To family and care givers who might be providers.
3. To the providers of housing, medical, education, and/or transportation.
4. To lend money to others, including the cost of remodeling a house for the benefit of the DB, allowing the trust to enter into a deed of trust note as security for reimbursement on sale.

K. Removal of Trustee.
1. The trust should provide some mechanism to remove trustee and appoint another trustee unless the successor is already named in the document.
2. Normally, the power to replace is given to an independent third-party (the trust protector) who has some knowledge of the DB, but also will not benefit directly or indirectly from the removal of the trustee.
3. Providing for removal of a trustee based on some standard or condition is not recommended given that such cannot adequately anticipate every issue.

L. Trust Protector or Advisor.

1. Authority Over the Trust. A trust protector should be named and granted either broad or limited powers over the trust to replace a trustee or change or amend the trust if there is a change in the circumstances or needs of the DB or there is a change in the applicable state or federal laws either affecting Benefits or taxes.
2. Authority Over the DB. Consider naming a person who might be solely responsible for the care and well being of the DB, including the enforcement of legal rights (either to appoint or serve as the guardian *ad litem*), and authority to replace and appoint a new guardian, or to force a change in the level or location of care.

M. *Crummey* Power Issues:

1. The creation of *inter vivos* third-party trust will normally be funded either by a taxable gift or by a gift that qualifies for the annual gift tax exclusion ($12,000) as a present interest gift if the beneficiary(-ies) is given a valid *Crummey* power.
2. If the DB has the capacity to exercise/waive the *Crummey* right, he/she can do so with his own authority. If the DB does not have the requisite capacity to exercise/waive his/her *Crummey* right, then the right can be exercised/waived by a natural guardian if the DB is a minor or the legal guardian if the DB is over the age of 18.
3. Exercise caution when using *Crummey* powers.
   a. The *Crummey* power must be a present and real power to withdraw and not be illusionary.
   b. Granting a DB a present right over the gifted-assets using a *Crummey* power may result in the gift being treated as a countable resource and thus adversely affect Benefits. This result may occur as to either amounts actually withdrawn or as to amounts forgone when the *Crummey* right is waived.
   c. Under the ruling of *Chistofani*, it is possible to not give the DB a *Crummey* power and instead grant the *Crummey* power only to the other trust beneficiaries.[45]
   d. Although in-depth *Crummey* planning is beyond the scope of this outline, it is normal to limit any real *Crummey* power to an amount that is the lesser of $5,000 or 5% of the gift to avoid giving the *Crummey* power-holder a general power of appointment which may result in adverse federal gift and or estate tax issues.

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[45] Given that the trust will typically also name residual beneficiaries who are family members (or allow sprinkle distributions during the life of DB), under *Christofani* such residual or sprinkle beneficiaries may also be given a present right of withdrawal, thus qualifying the transfer as a present interest gift. Note: The IRS recognizes *Crummey* withdrawal powers only if they are held by trust beneficiaries with nondiscretionary income interests or vested remainder interests in the trust. The IRS will not allow the annual exclusion for a transfer subject to a withdrawal power held by a contingent beneficiary or by an individual who has no other interest in the trust (a so-called "naked" power). The Tax Court, however, has rejected this approach and recognizes the use of a *Crummey* power to enable an annual donee exclusion for a withdrawal right held by a contingent remainder beneficiary of a trust. See: *Estate of Christofani v. Comr.*, 97 T.C. 74 (1991), *acq.*, 1992-1 C.B. 1, *acq. in result only*, 1996-2 C.B. 1.

N. Early Trust Termination and Amendment Provisions:

1. Consider adding an escape clause ("poison pill" clause) allowing either the trustee or trust protector/advisor to terminate the trust early if a creditor is successful in piercing the trust or the mere existence of the trust adversely affecting the DB's entitlement to Benefits. The remaining trust estate can then pass to the residual beneficiary(-ies), or to one specific person, free of trust, with the hope or goal that person will hold the funds as an "informal trust" for the benefit of the DB.[46]
2. If there is either some likelihood in the future that the DB may no longer need Benefits or that Benefits may no longer exist, then authorize the trustee to either terminate the trust or authorize a switch to an ascertainable standard that allows for support-type distributions.
3. Consider giving the trustee or trust protector the authority to amend the trust if there is a change in the law, applicable Benefits, or the future needs of the DB.

O. Remainder Provisions:

1. On the death of the DB, the remainder of the trust estate should not pass to the estate of the DB.
2. The trust must provide a named person or entity that will receive the remainder of accrued income and undistributed principal on the death of the DB.
3. Remainder interests can pass to other children, grandchildren or one or more charities.
   a. If the remainder can pass to a skip person, allocate GST exemption to this trust to avoid a GST tax.
   b. If a remainder beneficiary is a qualified charity, no charitable income or estate tax deduction will be allowed given that the trust is no a charitable remainder trust as defined within IRC §643.

P. Powers of Appointment and Related Trustees:

1. In general:
   a. IRC §2041 provides that a <u>general</u> power of appointment (GPOA) may be created whenever the trustee has the unlimited discretionary authority over assets that can be used to benefit himself.[47]
      (1) The value of the property that is subject to the GPOA will be included in the power holder's gross estate on death pursuant to IRC §2041.

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[46] Care needs to exercised in drafting such a provision to avoid an unintended transfer tax consequence to the trustee-beneficiary. If the trustee-beneficiary has the power to terminate the trust and appoint the remainder to himself or to one that he has an obligation to support, this will be a general power of appointment. See discussion below re: Power of Appointments.

[47] A GPOA is a power under which the holder of the power has the authority to appoint the property that is subject to the power in favor of anyone, including himself, his estate, his creditors or the creditors of his estate. No GPOA is created if the exercise of the power is: (i) limited to an ascertainable standard; (ii) exercisable only with the creator of the power; or, (iii) exercisable only in conjunction with a person holding an adverse interest in the property that is subject to the power.

(2) A limited or special power of appointment (LPOA) is any power that is not a GPOA. Generally a LPOA is a power that cannot be exercised to benefit oneself and can only benefit others. A LPOA is not included in the power holders gross estate on death.

b. No GPOA is created if distributions from the trust are limited to an ascertainable standard ("health, education, maintenance and support");[48] however, an ascertainable standard cannot be used in the context of a third-party trust for a DB given that such creates a requirement of support, subjecting the trust estate to being an available resource.

c. A general power of appointment can inadvertently be created when the trustee is also a residual beneficiary of the trust; for example:

(1) The trustee has the unlimited discretion to not distribute funds to DB, resulting in a bigger pot for the remainder beneficiaries to enjoy on the death of the DB.

(2) The trustee has the authority to terminate the interest of the DB in the trust and the remaining trust estate is to be distributed to himself and his siblings.

2. Naming a Trustee who is a Beneficiary:

a. Common Facts: Parent creates a testamentary third-party trust that provides discretionary supplemental distributions only to Daughter (the DB) for her life, with remainder to Son, and names Son as trustee.

b. Q: Does the above create a GPOA in S given that if he fails to make distributions to D, he benefits in the end by getting more?

(1) A: Yes. Because S is both the trustee and a remainder beneficiary with the discretion to make distributions not limited by an ascertainable standard, it is possible that a GPOA has been created.[49]

(2) A: No. It is arguable that despite the "discretion" given to S, he still must act as a fiduciary and cannot take action in his fiduciary capacity that would intentionally benefit himself to the detriment of D, although he could make decisions that could be a detriment to S for other reasons.

c. Same facts, but trustee also has the authority to make discretionary distributions to <u>other</u> beneficiaries during the life of the DB (*i.e.*, authority to "sprinkle" the income and/or principal among the siblings). The trust should be drafted to provide that the authority to make distributions to the siblings should be limited to an ascertainable standard to avoid a GPOA. Thus, distributions would

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[48] IRC §2041(b)(1)(A); Regs. §20.2041-1(c)(2).

[49] However, this will likely be a non-issue given that the fair market value of the GPOA may in fact be nominal. For example: P creates a purely discretionary supplemental needs trust for the life of DB, naming S as both the trustee and as the remainder beneficiary. Assume DB has a normal life expectancy. If DB is 22 and S dies, what is the value of the GPOA to be included in S's estate under §2041 given the continued discretionary distributions to DB during her life? If DB is 89 and S dies, what is the value of the GPOA?

be allowed to the DB based on supplemental needs and no ascertainable standard, but distributions during the life of the DB to other beneficiaries of the trust would be limited to an ascertainable standard.

3. If the trust includes an Early Termination Clause (see IV.N., above), consider using one of the following to prevent the trustee-beneficiary from having a GPOA:
   a. Draft the trust so that if there is an early termination of the trust, the person making the determination to terminate the trust is excluded from taking as a remainder beneficiary.
   b. Draft the trust to allow for the early termination of the trust only with the consent of a person who has a substantial interest in the trust estate which is adverse to the power holder.[50] Thus if either the consent of the DB or the DB's legal guardian is required to terminate the trust, the trustee's discretionary authority to terminate the trust should not be treated as a GPOA but rather only as a LPOA.
   c. It is possible that a court's determination that the trust estate will be subject to the creditors of the DB or there will a loss of Benefits, is in itself an ascertainable standard.[51]
   d. Draft the trust so that only the life interest of the DB terminates, and the remaining trust continues for the remainder beneficiaries in some manner with all distributions subject to an ascertainable standard.
4. Consider adding a savings clause in an attempt to negate the inadvertent creation of a GPOA. For example:

> Notwithstanding anything in this document to the contrary, a person who is a beneficiary under this document shall not have any power that will cause the property to be subject to a power of appointment that would be included in such beneficiary's gross estate under IRC §2041.

V. ADDITIONAL CAVEATS.

A. Impact of Other Estate Plans.

1. The client should advise grandparents and other family members (*e.g.*, great-aunt Edna who has no children) to make appropriate plans to minimize the negative impact of leaving assets to a DB. This is especially important

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[50] IRC §2041(b)(1)(C)(ii). If the power is exercisable only with a non-adverse party, the power will be a GPOA.

[51] This result is not guaranteed and the author is not aware of any rulings supporting this interpretation. It would be appropriate to draft such language to make it clear that the court has <u>only</u> the right to determine that either (i) a creditor of the DB can take the assets of the trust, or (ii) the trust will adversely impact the DB, and that the court does <u>not</u> have the right to terminate the trust and the discretionary authority to terminate the trust is left to the trustee. Thus the termination provision might provide a condition precedent that provides that if a court or other governmental agency determines that a creditor has access to the trust estate or the Benefits of the DB are to be reduced because of the trust, then the trustee has the authority to act. See Cline, *Powers of Appointment – Estate, Gift and Income Tax Considerations*, BNA Tax Management Portfolio 825-2nd, at III.C.3.

for grandparents and others who might inadvertently leave funds to the DB either directly or as result of the death of another, *e.g.*, grandparent provides in his dispositive provisions: "All the rest and residue to my son Joe if then living, and if not, then to his issue, *per stirpes,*" and Joe leaves a child who is disabled.

2. A corollary to the above is to consider those who might benefit from the client's estate who are outside of the client's normal traditional family unit — great grandchildren, nieces, nephews, etc. Thus, it is appropriate to ask whether any of the designated beneficiaries named in the estate plan (*e.g.*, "to the then living issue of my cousin Jane"), have any health or disability concerns.

B. Multi-State Concerns. When DB lives in another state, carefully consider application or impact of other state laws on the Alaska testamentary trust. Clearly make the testamentary trust subject to Alaska spendthrift provisions and provide that Alaska law shall govern. Although a majority of jurisdictions protect third-party discretionary spendthrift trusts, a minority of states may pierce such a trust based on public policy allowing creditors to take the assets to cover the cost of care.

C. Future Planning.

1. Even though there may not be a current third-party trust planning issue when you first meet with a client, the need for a third-party trust might develop in the future. Therefore consider whether current estate planning documents should grant a fiduciary the discretionary authority to create and fund a third-party testamentary supplemental needs trust for a beneficiary who might be disabled.
2. Add to your will-review reminder letter that clients should consider third-party trust planning issues in the future as more decedents are born and as circumstances change in their lives and the lives of their intended beneficiaries.

D. Designation Beneficiary Forms. Advise the client in writing to change all designation of beneficiary forms (life insurance, retirement plans, IRAs, etc.) to be consistent with the client's estate planning goals.

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