LEIMBERG'S

THINK ABOUT IT

Diversity of opinion helps us be more successful! Your Success Matters! Therefore Prudential is pleased to provide you with material that offers different views and opinions on various subjects. Please note that these opinions are not necessarily those of Prudential. Leimberg's Think About It is distributed as a courtesy to our representatives at The Prudential Insurance Company of America. Prudential expressly disclaims responsibility for any content and advises that your clients should consult with their accountant, tax advisor and/or legal advisor to confirm the accuracy of these analyzes and for advice concerning their particular circumstances.

THE CHOICE IS YOURS

In the 40 years I have been involved in estate planning, I don't think I have ever seen the depth of passion or the diversity of opinion that the Terri Schiavo tragedy had engendered earlier this year among professionals and planners who deal with "life and death" issues in their practices. For the professionals, the Schiavo case brought concerns about the proper role of courts, government agencies, and legislatures in resolving disputes vis-à-vis extremely personal (and private) decisions, as well as how it may affect the use of living wills, health care directives and other planning devices/documents.

For the general public, the developments of the case also elicited intellectual, emotional opinions (at times, very strong and highly charged) about treatments and measures that are used (or acceptable) in extreme and end-of-life medical situations. While the case may have heightened our clients' awareness of the need to plan in advance for their medical/health care; nevertheless, some are probably still confused about the necessary steps they need to take to protect themselves and their loved ones, as well as to prevent (or minimize) regrets or tragedies (such as the one faced by Terri Schiavo's husband and her family).

This commentary is a frank discussion of living wills, health care proxies, durable powers of attorney, Medicaid and trusts, and revocable living trusts.

It emphasizes the need to address the issues dealing with mental/physical incapacity, obligations of caring for a disabled relative or loved one, or providing a residence to the physically incapacitated. It also stresses the economic impact of a principal income producer's incapacitation, and the involuntary and often drastic financial and emotional adjustments that inevitably occur and affect the family. It is essential that these difficult issues are faced – before it is too late, and important planning options are lost.

I frequently address consumer groups (clients/prospective clients) and speak about these problems and offer potential solutions they should consider for their particular situation.

The following is a sample of my presentation that also contains many useful comments and suggestions on the design and wording of certain key documents. You can use the material as guideline for a client-oriented seminar.

THE CHOICE IS YOURS

(SAMPLE CLIENT PRESENTATION)

TIME IS OF THE ESSENCE

You may be one of the many individuals who are concerned about the issues of mental or physical incompetence, obligations of caring for a disabled family member or loved one, or providing a residence for someone who is physically or mentally incapacitated. If you are a principal income producer and you become incapacitated, financial and emotional adjustments (at times sudden and drastic) will occur – just when you and your family are least capable of coping with them.

When long-term public or private institutionalization is required, your property may be depleted (or you may have to expend all or almost all of your assets) before you will be eligible for governmental or public aid. Should you become terminally ill and incompetent, you may forfeit the right to prevent "heroic efforts" to continue your life no matter how useless the efforts may be. Or, you may have strong feelings that such efforts should be made no matter what the potential outcome.

None of these are pleasant thoughts.

But face them you must!

And you must address these and other issues before it is too late and many important planning options are lost. To preserve and protect your property and your dignity, to express your wishes, as well as assure your family's financial well-being, you must act now!

If you are concerned about these issues – and are interested in learning more about the potential solutions – keep reading.

LIVING WILL

If you were so ill or unconscious, or, for any other reason, were unable to make (or communicate) your own decisions regarding health care, who, if anyone, would you want to make such decisions? A so-called "Living Will" may be part of the solution.

What is a living will? A living will (also known as an "Advance Directive for Medical Care") is a document that allows you to express, in advance of a terminal illness, what treatment would (or would not) be acceptable to you. It is limited in scope, such that it only covers three situations: (a)

if you are in a coma, (b) if you are in a persistent vegetative state, or (c) if you are close to death. For example, your living will might specify that – in the event death is imminent, or the loss of mental capacity is inevitable, substantial, incurable, irreversible, and you were left with no hope of recovery – extraordinary, or artificial life-sustaining techniques should not be used to prolong your life.

Our state has [does not have]* "Right to Die" laws recognizing the validity of your right to choose to forgo specified medical treatment in specified conditions. Your declaration of desires, if properly executed while you are legally competent, will help your family and physicians follow your wishes – and make it immeasurably easier for them to do so in every respect.

*[NOTE: State laws may vary – adjust your talk accordingly to comply with applicable state statute.]

What is absolutely clear is that a spouse, parent, sibling, or friend will not be allowed to make a life-determining decision on your behalf – unless you have provided clear and convincing directives that such action conforms with your expressed desires. A living will is certainly one way to express those desires.

Here are some suggestions to discuss and consider with the attorney who drafts your document. Since each state's law may differ from the law of others, it is essential that your attorney draft this document to comply – at the very least – with your state's laws. Better yet . . .

- The document should meet not only your state's law but also the most stringent requirements of any state's law with respect to:

  (a) The number of witnesses. (I suggest 3 adults.)

  (b) The "competency" of a relative, or potential beneficiary, or person, who may be responsible for the costs of your medical care to sign as a witness. (I suggest you choose someone other than a relative or beneficiary to sign as a witness.)

  (c) The necessity of renewing the document in order for it to be effective. (I suggest you check with your attorney at least every three years to assure the living will is still effective.)

  (d) Signature and notarization requirements. (I suggest you sign and your signature should be notarized. Your witnesses should sign in the presence of each other and the notary public.)

- Be sure to state in the document the following:

  (a) It is intended to be a legal document.

  (b) You are of sound mind at the time of signing (consider a video or audio tape of the occasion, if necessary).

  (c) You are making the declaration willfully and voluntarily.

  (d) You have a specific desire to avoid extraordinary measures or artificial means to prolong your life. And

  (e) In the event of a diagnosis of terminal illness or disease, instructions as to the withholding or withdrawing of life-sustaining treatment are indicated.

- Do not sign the document unless you are absolutely sure you understand and agree with each and every term or phrase (a knowledgeable and competent attorney – particularly in this area of the law – will define each term in the document and review it with you paragraph by paragraph). For instance, the term "an incurable or irreversible condition which is likely to cause my death within a relatively short time" should be defined and/or an example given to avoid ambiguity.

- Consider exonerating those who comply with the document. You might say something to the effect that, "No physician, hospital, or other health care provider who withholds or withdraws life-sustaining treatment in reliance on this Living Will shall have any liability or responsibility to me, my estate, or any other person for having complied with this document."

- Authorize in your living will one (or more) specific person(s) to "interpret" words or terms in the document if necessary.

- Give copies of your living will to your personal doctor and make sure that copies be kept in your medical records. Request that copies also be held in your hospital or nursing home medical files. Appropriate family members should also be given copies.

HEALTH CARE PROXY

A "Health Care Proxy" (also called a "Durable Power of Attorney for Health Care") has been authorized in many states by specific law. A health care proxy can be broader and more flexible than a living will, since it provides for many types of health care decisions other than those regarding life-sustaining treatment. It allows you (a "principal") to appoint someone (an "agent") to make "any and all health care decisions" on your behalf in the event you are unable to make (or communicate) your own.

A health care proxy is sometimes used in addition to a living will. Or it may be broad enough to take the place of a living will – for instance, if the language of the living will is included in the health care document (and the applicable state laws allow the use of a single, combined document).

You, of course, continue to make decisions as long as you are able to do so. You can consent, or refuse to consent, to any health care treatment or medical procedure, and the authority you give to your agent can be revoked orally or in writing.

Here are some suggestions to consider with your attorney:

- Think about including special instructions for medical treatments or procedures such as artificial nutrition and hydration (nourishment provided by feeding tubes), cardiac resuscitation, blood transfusions, antipsychotic medication, kidney dialysis, transplantation, electroconvulsive therapy, and psychosurgery.

- If your state has a specific law on health care proxies, the provisions of your document should follow or closely approximate the state's language. Or better yet, it should conform to the most stringent of any neighboring states or where you are likely to vacation or retire.

- Have the document witnessed by at least 3 individuals totally unrelated to you (none of whom is the agent named in the proxy) in the presence of a notary public who notarizes the signing. Include their addresses and phone numbers. Appoint alternate "agents" in case the one you have chosen cannot or will not serve. Include the addresses and phone numbers of all agents in the document.

- Check with your attorney as to the effective duration of the document. (Some state laws put a limit on how long such documents are effective.) Ask your attorney to establish a "tickler" file to warn you when your health care proxy needs to be renewed.

- Execute several "originals" and give one to (a) your designated agent, (b) your doctor, and (c) your attorney. Put a note in your wallet stating that you have signed a health care proxy and/or living will, and give the name(s) and phone number(s) of the person(s) who holds (or hold) the document(s). You can stipulate a given date or condition upon which the proxy will expire. Absent such a date, the proxy remains in effect until revoked (unless state law provides otherwise).

DURABLE POWER OF ATTORNEY

A "Power of Attorney" is a relatively simple and inexpensive legal document by which you give a spouse, child, or other relative or someone else (the "attorney-in-fact") the right to act in your place on your behalf with respect to financial matters. You can make this power as broad or as narrow as you wish.

Be sure your document states that the power is "Durable." This means the power you give your agent is not affected by your subsequent disability or incapacity. (Each state has different "magic" words that are required to make the power "durable.") Of course, you must be mentally competent in order to create a power but physical disability is not a hindrance. Every state recognizes a durable power of attorney.

For many people, a well-drafted durable power of attorney is important as a will. It may negate the need to petition a court to have a guardian or conservator appointed to handle your assets if (and when) you are unable to. It is a "must" if you are currently suffering from a physical disability or illness that could lead to permanent or long-term incapacity. However, it should be considered by healthy individuals who would like to provide for continuity of management of assets if – for any reason – they cannot manage their assets or handle their own affairs for a period of time. A power of attorney does not become "stale," it remains valid until you die, or unless you specifically provide for a time limit.

Have your lawyer draw up a durable power of attorney now – while you are legally competent. Your attorney-in-fact can be anyone you choose (but typically not the lawyer who drafts the document) who is of legal age at the time the power is exercised. That person can invest, reinvest, and manage your assets on your behalf just as you could. Appoint alternate "agents" in case the one you have chosen cannot or will not serve. Include the addresses and phone numbers of all agents named in the document.

Consider with your lawyer about the following:

- Provisions allowing your attorney-in-fact to do the following on your behalf:

  (a) file income, gift, and other tax returns,

  (b) obtain access to safe deposit boxes,

  (c) deal with retirement plans,

  (d) deal with insurance companies,

  (e) make gifts (either outright or in trust) up to the amount of your annual exclusion to the persons named in your will and/or your spouse, children, or other descendants.

- Check with your bank (or other financial institutions) and confirm that they will recognize the power. For example, some banks have their own forms, but a number of states have enacted standard forms of powers of attorney which banks must accept and honor. In this case, the bank will be held liable if you incur damages because it refuses to honor the power given to your attorney-in-fact.

- The document should be signed by the person to whom the power is given (your attorney-in-fact or agent) and his/her signature notarized in order to authenticate his or her signature and authority. Have 3 witnesses sign the document.

- Provide, where the agent is your spouse, that upon a divorce or legal separation, the agent (your ex-spouse) is deemed to have resigned in favor of the alternate agent you have named in the power.

MEDICAID AND TRUSTS

Medicaid is a federal and state financed assistance program for certain needy and low income persons regardless of age. It is governed by state laws (varying from state to state) within broad federal guidelines. This is a very important program in terms of preserving your assets since it covers almost all essential medical care costs once you qualify.

Medicaid is based on the amount of your income and capital resources; the more you have the less likely you will qualify for Medicaid. Worse yet, your state's laws may make you ineligible if – within a specified period of time – you transfer more than a specified amount of assets in order to protect those assets and become eligible for Medicaid. Furthermore, if you are married, your spouse's income and assets are treated as if they were yours. Generally, this "deemed ownership" rule makes it more difficult for couples (both of whom have income and assets) to qualify for Medicaid. A cynical (but realistic) way to view this is that you and your spouse must both be "impoverished" in order for either of you to qualify for Medicaid.

Can you transfer assets to your children and/or grandchildren to meet the resources test? The answer is: In the event you are institutionalized in a medical institution or nursing facility, Medicaid law requires a state to delay your eligibility for benefits if it is determined that you transferred assets for less than full consideration (i.e., the fair market value) within a certain period of time prior to the day you applied for Medicaid benefits. The "look back" rules pertain to transfers in general made within 36 months prior to the date of application for Medicaid benefit; and to transfers in trusts made within 60 months. And there are many practical reasons why, over and above the law, you should not transfer assets to your children to sidestep Medicaid eligibility rules.

So what can you do? Think twice and think twice again before transferring your assets. First of all, you are making an irrevocable transfer. So you **cannot** change your mind and **reverse** the transfer. And, once the property is owned by someone else, their creditors or ex-spouses might get it, or they might manage/invest the property poorly or spend it unwisely, or they might die and leave it to someone other than you. Once they own property you have given them, the recipients are under **no** legal obligation to give it back to you, or even use it on your behalf or for your benefit. Furthermore, you are also making a gift that may be subject to current gift tax.

But, if you do decide to transfer property to your children, grandchildren, or others, you must make your gift more than 36 months (or 60 months to a trust) before you apply for Medicaid. If you are already in a nursing home (or you are about to go into one), you may want to consider keeping enough assets to pay for your care for the next 36 months. Then, you may consider transferring some or all of the remaining assets (while paying your expenses), and apply for Medicaid 36 months after the date on which you make the last of your asset transfers.

Medicaid Qualifying Trust. Slimming down your estate (and reducing your assets/resources) for Medicaid eligibility can be accomplished through outright gifts or in trust – provided gifts are made 36 months (or 60 months for transfers to trusts) prior to the date of your application for Medicaid. There may be both federal and state gift tax implications to either type of gifts. If you make the transfer to a revocable living trust, it remains your asset for not only income and estate tax, but also Medicaid eligibility purposes. So this type of transfer will not accomplish your objectives.

Can you have your cake and eat it too? Can you set up an irrevocable trust which will provide you with benefits without disqualifying you for Medicaid benefits?

Generally, the answer is "**NO**." The law specifically addresses what it ironically calls the "Medicaid Qualifying Trust." It is ironic because a trust which meets this definition will disqualify you for Medicaid benefits. If you create a trust (revocable or irrevocable) for your (or your spouse's) benefit, even if only the trustee has the right to determine whether or not you receive income or principal from the trust, you are treated as if you have retained an amount equal to the maximum income or principal the trustee could possibly distribute to you. The result is the same even if you never get a dime from that trust, or even if you can prove you set up the trust for some reason other than to circumvent Medicaid rules.

On the other hand, if the trust is drafted to specifically prohibit the trustee from ever distributing principal to you, no matter what the circumstance or how dire your needs are, you can limit the amount considered as yours for Medicaid eligibility purposes. This assumes the law in your state also agrees that there is no way you can get that principal, or have it used **on** your behalf.

"**Luxury Trust.**" A trust may be valuable – even if it does **not** fully accomplish the "have your cake and eat it too" objectives. For instance, the trust can be drafted so that it is a "Solely Supplemental to Medicaid Trust." Some attorneys call this a "Luxury Trust" since it would provide only comfort items and luxuries such as cigarettes, birthday presents, or others to help make your life more pleasant, but which would not provide you with food, clothing, shelter, medical care, or any other basic necessities.

The trustee of the luxury trust would be specifically prohibited from using either trust income or assets for basic support. In other words, you will receive income and/or principal only to the extent of expenses not covered by Medicaid, or in a way that does not preclude public benefits.

So you can assure payment of your special needs without depriving yourself of Medicaid benefits, or allowing the state to invade your trust and take its assets. Of course, the trust may also provide professional management of your assets/investments (placed into the trust) and can serve as an alternative to guardianships or conservatorship.

Although the luxury trust technique may work in some states, at least one state (New Jersey) provides that "Any provision in a contract of insurance, will, trust agreement or other instrument which reduces or excludes coverage or payment for goods and services to an individual because of that individual's eligibility for or receipt of Medicaid benefits shall be null and void, and no payments shall be made under this act as a result of any such provision."

It is likely that Congress only intended to prevent voluntary transfers intended to avoid the reach of Medicaid laws. When the beneficiary of a trust (e.g. a parent or child) did not set up the trust or put the assets into the trust and cannot compel the trustee to pay out income or principal for any reason, neither federal nor state law (its letter or intent) should be violated by the "Luxury Trust," or "Third-Party" and "Convertible Luxury" Trusts (described below). But it would be imprudent to make a blanket assumption about that. As I have mentioned throughout this discussion, state laws will vary widely and you must seek specific advice from competent local counsel.

"**Third-Party" and "Convertible Luxury" Trusts.** Third parties such as a son or daughter can much more safely set up luxury trusts for you. Such trusts can give the trustee the discretion to make distributions to you or other specified beneficiaries and "sprinkle" or "spray" trust income and principal as needed by each and all of the named beneficiaries. The trust could be "convertible." It could provide you with income and/or principal for food, clothing, shelter, medical care, or any other needs until you enter an institution, or begin to receive "in-home" or other out-patient care. At that point, the trust would convert to a solely luxury trust. The trust could provide that at your death, the remaining unexpended trust income and/or principal would be paid to the other trust beneficiaries (these are called "remaindermen").

REVOCABLE LIVING TRUST

When the assets in your estate are complex, a revocable trust is often indicated in conjunction with a durable power of attorney and other planning tools or techniques. A revocable living trust can enable you to keep control as long as you are able to – by serving as the initial trustee. If you should become incapacitated, the successor trustee would assume the responsibility of investing, managing, and conserving the property on your behalf and for other trust beneficiaries (e.g., your spouse and children).

A revocable trust is one that allows you to change your mind and regain asset/property that you have put into the trust, or change the terms of the trust, or revoke the trust. The terms of the trust never become public knowledge (either during your lifetime or at your death) nor does the public have the right to know how much is in the trust. Only you, your trustees and beneficiaries will have access to the trust instrument.

As is the case with any planning tools or techniques, there are costs, downsides, and negatives to a revocable trust. For instance, because you retain complete control over the assets in the trust, for federal and state income and estate tax purposes, you continue to be treated as the owner of the trust assets. So, you'll be taxed on the trust's income and the assets will be includible in your gross estate for estate tax purposes. Furthermore, the assets in a revocable living trust will be subject to the claims of your creditors.

Once again, as with all of the comments I have made, it is essential that you consult with your attorney to review the relative advantages and disadvantages of revocable living trust for your particular situation.

CONCLUSIONS AND FINAL SUGGESTIONS

- Major medical, basic health insurance coverage, disability income insurance, and long-term health care insurance are an ever growing necessity for those who wish to live with dignity and independence from governmental aid or public assistance. Make sure you have adequate coverage and it is the right type for you.

- You should have an up-to-date durable power of attorney to eliminate the need to have a guardian, committee, or conservator appointed on your behalf to handle your affairs (such as pay your bills and perform other acts on your behalf).

- Consider – if you deem it appropriate – a Living Will and/or a Health Care Proxy. Think about the good that may come of anatomical gifts and the reduced anxieties and burdens from a thoughtfully written letter of instructions to those whom you want to carry out your desires.

- Consider a revocable living trust – in addition to an up-to-date will – to provide for management of your assets and financial matters.

- Consider an irrevocable trust to protect your assets from the claims of creditors, save state and federal taxes, and perhaps (if state law allows) provide income supplementary to Medicaid in the form of a Luxury Trust.

- Be sure all your important papers are in one place (preferably a safe deposit box) where a selected person can find them. Include the names and phone numbers of financial advisors such as insurance agents, CPA, attorney, banker, and others upon whom that person can rely, as well as the locations of bank accounts and other assets. Also include the names, addresses, phone numbers of all your family members who are named as beneficiaries under any life insurance policy, your will, or employee benefit plan.

REMEMBER:

YOU CAN CHOOSE TO TAKE ACTION NOW AND KEEP CONTROL

OR

YOU CAN CHOOSE TO HESITATE – DO NOTHING –

AND LET STATE LAWS AND FATE

CONTROL YOU.

IT'S YOUR CHOICE!

FINAL WORDS . . .

Without a doubt, end-of-life issues are most unpleasant, difficult and painful to address, but they are part of our clients' overall planning process. We, as advisors, have an obligation to help our clients with compassion in achieving their end-of-life wishes with dignity. To that end, we must listen to their concerns, respect their opinions and focus on their objectives – even when theirs may be contrary to ours. We must help them make informed decisions about very highly personal and emotionally charged issues – objectively, and in a timely manner. Time is indeed of the essence, and the time to plan for disability, incompetence, and death is ahead of time. As my friend and colleague Andy DeMaio said so aptly, "We must assure each of our clients that he or she will not lose his or her voice concerning end-of life decisions."

Prudential Financial