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## **Expecting the Unexpected – Incapacity Planning and the Need to be Prepared**

The recent news stories about Sumner Redstone and his empire highlight an increasing problem in 21<sup>st</sup> century America – the importance of planning for incapacity. Redstone, the 92-year old chairman and largest shareholder of two public companies, Viacom and CBS, is currently the subject of litigation in California alleging that he is incapacitated and unable to manage his affairs.

Redstone is hardly alone. In the United States, 1 in 9 people age 65 or older have some form of Alzheimer’s disease. About one-third of people age 85 or older are so afflicted.<sup>1</sup> These statistics, combined with the fact that Americans are living longer and are having smaller families, mean that planning for incapacity has become just as important or even more important than estate planning at death.

In the absence of planning, when a client begins to lose the ability to make decisions a family is faced with a dilemma. Court proceedings to establish incapacity vary from state to state but they tend to be complex and costly. They usually involve, at a minimum, presenting medical and psychological evidence in court, and the court designating someone (often referred to as a *guardian ad litem*) to act in the proceeding on behalf of the incapacitated person. Courts are understandably reluctant to deprive people of their legal rights by declaring incapacity, but the process can be painful for the family and demeaning for the incapacitated person. On the other hand, having an elderly person of doubtful capacity execute planning documents to avoid these burdensome court proceedings can present equally challenging problems, especially if there are different views within a family about who should make decisions for the person.

What are some of the tools that clients can use to plan in advance for their own incapacity?

The best tool is one that many clients should already have as a key part of their estate plan – the *Revocable Trust*. Revocable trusts have become a popular alternative for wealthy clients to creating a Last Will and Testament. They offer advantages in terms of privacy and flexibility, and they enable clients to avoid probate proceedings in local courts at death. But Revocable Trusts offer another advantage over Wills – they can address not only what is to occur at death, but also

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<sup>1</sup> Alzheimer’s Association. 2015 Alzheimer’s Disease Facts and Figures.

what happens during lifetime in the event of incapacity. In a Revocable Trust a client can define the following:

- At what point should he or she be considered to be incapacitated? What is the standard for incapacity?
- Who is responsible for making the decision about a client's incapacity? Is this one person (such as a personal physician), or is more than one opinion required?
- Who can benefit from the trust once a determination of incapacity has been made? Just the client, or the client's family as well?
- What happens if the client's incapacity ends, and who makes this determination?
- Most importantly, in the event of a determination of incapacity, who is to have control of the trust assets as trustee? One or more successor Trustees should be designated to take control of the trust.

A well-crafted revocable trust will create a customized contract that addresses all of these points, and will enable each client to create a plan for incapacity that stands beside the client's estate plan addressing what happens at death.

But creating a Revocable Trust with suitable provisions is only part of the solution – assets must be transferred to the Revocable Trust prior to the client becoming incapacitated. Since the client is usually the initial Trustee of the Revocable Trust (prior to incapacity), this means a client's assets should be retitled from individual name to the name of the Revocable Trust. It may be impossible or impracticable to re-title some assets (such as assets in qualified plans or real estate subject to a mortgage), but the goal of the planner is usually to retitle as much of the client's wealth as possible into the name of the Revocable Trust.

Another key document in planning for incapacity is the *Durable Power of Attorney*. Revocable Trusts only have application to the assets held within them. A Durable Power of Attorney, in contrast, enables a client (referred to in this context as the "principal") to designate one or more persons (referred to as "agents" or "attorneys-in-fact") to act on his or her behalf in a broad range of business, financial and personal matters.<sup>2</sup> The "durability" of a power of attorney refers to the fact that it remains in effect even though the principal later becomes incapacitated. Powers of attorney are usually structured to give the principal a long list of powers that can potentially be granted to the agent, covering matters like bill paying, preparation and filing of tax returns, dealing with insurers, etc. The principal can include specific powers and exclude others, or can simply choose "all of the above."

Many powers of attorney are "presently exercisable," meaning that authority is granted to the agent as soon as the power of attorney is signed by the principal. Some states, such as New York, also permit a principal to execute a "springing" power of attorney that only becomes effective in the event of incapacity. This type of power of attorney is intended for clients who are not comfortable giving their agent authority over their assets currently. However, many planners feel that the conditions required to trigger a springing power make them cumbersome in actual use. What many choose to do as a practical matter is sign powers of attorney that are presently exercisable, but keep the signed documents with their attorney so they are only used when needed (and not before then).

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<sup>2</sup> Clients usually sign a separate document referred to as a "Health Care Proxy" or "Health Care Directive" that designates one or more persons to make medical decisions in the event of incapacity.

A critical point to make in this context is that both a successor trustee of a Revocable Trust during incapacity, and an agent acting under a Power of Attorney, are *fiduciaries*. A trustee or an attorney-in-fact is always required to act in the best interests of the trust beneficiary/principal, to whom they owe a strict fiduciary duty. Law digests are full of examples of trustees and agents using incapacity as an opportunity to enrich themselves, and, when discovered, this can result in severe civil and criminal penalties. How is a client to protect himself or herself from the wrongdoing of their trustees and agents? What are the best practices in choosing a trustee or agent to act for you in the event of incapacity? Three thoughts come to mind:

- *Checks and Balances:* Although it may be easier to name a single individual to act for you in the event of incapacity, naming several persons to act as co-trustees or co-agents may provide a check against any individual fiduciary's wrongdoing or negligence. For example, a parent could name two children to act as co-trustees, or could name an attorney or trust company to act as co-trustee with a child.
- *Open Discussion:* Families rarely if ever discuss what is to take place in the event of the incapacity of a parent in advance of it actually happening. Discomfort in such discussions can be even greater than in talking about a parent's death, especially if the parent has been largely responsible for creating the family wealth. Talking openly within a family about what is to happen in the event of incapacity can set expectations and avoid unpleasant surprises.
- *Importance of Your Planning Attorney:* Finally, many clients do not understand that their planning attorney is more just than the draftsman of planning documents – he or she can be the champion of a client's intent and best interests. Including your planning attorney in the discussion of incapacity can reduce the risk of overreaching by fiduciaries and family members.

*HPM Partners works with its clients and their families to help them develop thoughtful, customized plans that address the challenges that come with age-related diseases and diminishing capacity. Reach out to your contact at HPM Partners for more information and to schedule a meeting or call.*

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