Hope for the Best, Prepare for the Worst

Planning for Possible Incapacity

by Alexandra Armstrong, CFP, CRPC, and Christopher Rivers, CFP, CRPC

The coronavirus pandemic we have lived through for the past year has many thinking about what would happen if we become too ill to manage our affairs. Our everyday lives involve a complex web of decisions regarding our families, health care, assets, liabilities and personal property. Should we be unable to handle our own affairs, someone needs to be able to make decisions on our behalf. So it's important for us to know what will be involved.

The centerpiece of any estate plan — and often the most difficult — is deciding which people you can trust to make these significant decisions should you be unable to do so. At the same time these people have to be willing to assume these responsibilities.

During your life, a trust and a power of attorney (POA) are the primary planning tools used to plan for incapacity. Below, we discuss what these terms mean, the responsibilities of each and the factors you should consider when choosing someone to act on your behalf.

At your death, your personal representative (PR) or executor takes on the same role. This person is often the same person as your trustee or POA. The duties of the executor are complex and will be covered in a future article.

Trusts and Trustees

First, some background on trusts and trustee duties. In its simplest form, a living trust is a legal document that enables you to title your assets in the name of a trust for your own benefit during your lifetime. In this case you are typically both the grantor (the one placing the assets in the trust) and the trustee (the one making decisions for the trust).

The trust also includes a set of instructions to be followed at your incapacity or death. These instructions are to be carried out by your successor trustee. Many choose spouses as their successor trustees, some choose banks or attorneys and some choose their children. Be sure you get the consent of the person who will act as a successor trustee and give the successor updated copies of the trust should there be corrections. Given the responsibility involved, it's important that everyone is on the same page.

A Trustee's Responsibilities

A trustee's primary responsibility is to follow the instructions set forth in your trust document. These will typically cover the manner in which the trustee should:

- **Provide the necessary cash flow** from the trust to meet your expenses;
- **Pay your bills** and obligations from trust assets;
- **Manage trust assets** in accordance with your wishes prior to incapacity and;
- **Ensure taxes** are filed properly for the trust assets.

In addition, the trustee is typically responsible for administering the trust assets at your death. Note that this role pertains only to the assets in the trust. For example, individual retirement account assets cannot be owned in trust and thus a trustee has no authority over them (more on this later).

After your death, we recommend the following procedure be followed:

- **The trustee should meet** with an estate-planning attorney and accountant to go over the trust document, trust assets and the trustee's responsibilities as soon as possible.
- **The trustee will need** to apply for a new employer identification number for the trust with the Internal Revenue Service.
- **The trustee must collect** all death benefits (Social Security, life insurance) and put them in a separate trust account until assets are distributed.
- **The trustee must notify** all financial service firms holding assets in the trust for which he or she is the trustee.
- **The trustee must keep** careful records of all trust expenses, verify and pay all bills and taxes of the trust, make a final accounting of assets and bills paid and give it to the beneficiaries.

If the assets are to stay in a trust after your death, your trustee will continue to oversee the trust and proper bookkeeping and reporting procedures will need to be established.

If the assets are to be fully distributed, the trustee needs to divide the cash and transfer titles according to the instructions in the trust and close the trust down.

Choosing a Trustee Wisely

We strongly recommend having one person serve as your successor trustee. Naming co-trustees means they must all agree on everything and sign off on everything, which adds difficulty and complexity to everyday tasks.

Choosing a family member, or even a close friend, as your trustee may or may not be the best choice. The trustee need not be a financial expert, but should be dependable and detail-oriented, with good, basic money skills, who knows when it's time to consult an expert

for assistance.

Using a Lawyer or Bank as the Trustee

If you aren't sure that you know someone who could function as a successor trustee you may select a corporate trustee, such as a bank trust department to fill the role.

It has been our experience that someone who knows your family may be a better choice to be the trustee. That person can consult a lawyer for advice on administering the trust. But every situation is different. If there's a chance that there will be a lot of family conflict, this might not be the best choice.

If you do choose a bank as a trustee, you have a viable trustee, and you will have an objective third party administer the trust.

However, corporate trustees such as a bank generally cost more than an individual trustee, and sometimes significantly more. In addition, bank trustees can be impersonal and unfamiliar with the deceased grantor's wishes or family dynamics.

Corporate trustees may be more inflexible because of increased liability and the fact that they must answer to their shareholders. But in a situation with the potential for disagreement within the family, it can be an advantage to have a neutral party who is not subject to outside influence.

Paying Trustees

As you can see, being a trustee isn't an easy task, and we think that the trustee should be compensated for this work. But it is fairly typical for a spouse or child to administer their loved one's trust for free. You have the right to specify how your trustee should be compensated in your trust document, to eliminate any ambiguity.

While many states have statutes limiting executor and attorney commissions in settling an estate, only about half a dozen states provide specific statutory fee schedules for trustees. It is not uncommon to see corporate trustees charge a fee of between 1% and 2% of the trust's assets.

Power of Attorney

Many people think that having a trust means they have taken care of planning for incapacity. But even if you have a trust in place, we recommend you have two durable powers of attorney: one to handle your financial affairs and the other to cover your health care directives.

This may be the same person as your trustee or executor, but you may also want to appoint different people.

Durable Financial Power of Attorney

A durable financial POA allows a person whom you have designated to act on your behalf when handling your financial affairs. This person may be called your agent or your attorney-in-fact.

You retain the right to modify or revoke the power at any time. A "standing" durable power of attorney becomes effective as soon as you sign the document; a "springing" durable power of attorney becomes effective under conditions specified in your document, such as incapacity. A durable power of attorney always ends at your death.

Note that a durable POA doesn't provide your attorney-in-fact with the ability to make decisions with regard to assets that are held in a trust. Only a trustee or co-trustee has the legal right to do that. In a case where you have assets in both a trust and an IRA account, the trustee would be responsible for the assets in the trust, while the POA would be responsible for the IRA.

If you're unable to make financial or medical decisions and haven't given anyone your POA, a family member may have to petition the court to appoint a guardian for you.

Health Care Power of Attorney

The health care POA enables you to provide guidelines and instructions about the extent of medical care and intervention you'd want under various circumstances. This isn't the same as a living will. It's more flexible than a living will since it allows for advance directives for a range of personal health care decisions, not just decisions regarding life-sustaining procedures. A durable power of attorney for health care can authorize access to medical records and assign responsibility for decisions regarding diagnostic procedures, specific treatments, pain relief, the right to employ or discharge medical providers and authorization for admission to or discharge from medical facilities.

This POA will be effective if your physical or mental condition makes it impossible for you to understand, make or communicate an informed decision about providing, withholding or withdrawing treatment. The person you name would be able to talk with your doctors and nurses about your care. Doctors and hospitals today have to follow strict privacy rules designed to protect personal information, but the unintended side effect is that without your written consent, they may not be able to discuss your condition with your loved ones, without a health care POA.

In your health care POA you can describe what quality of life is acceptable to you, thus relieving your family and friends of the burden of making these difficult decisions.

Today, many hospitals require that you have one of these powers in place before undergoing an operation. In some states, the individual designated for this responsibility must sign an affidavit stating that he or she will in no way financially benefit from your demise.

Planning for the Unknown

One of the key features of these documents is the ability to spell out your wishes and make clear how you would like your affairs managed. But the future is by nature unknowable,

Continued on Page 13

S&P 500 falls either 7% or 13% from its closing price the previous day before 3:25 p.m., trading gets shut down across all stock and future exchanges. A drop of that size after 3:25 p.m. would not trigger a trading halt. If the S&P 500 drops 20% or more from its previous closing price, trading shuts down for the rest of the day.

Overbought/Oversold

When the price of a stock jumps, someone who believes that it is due for a correction might argue that the stock is "overbought." When a stock or many stocks in a market decline steeply and suddenly, some might speculate that stock or the market is due for a rebound. When making such a prediction, one would say the stock or market is "oversold."

Panic Selling

When investors suddenly conclude that a security or market is doomed to a rapid price decline, they might engage in panic selling, offloading massive amounts of shares without necessarily doing thoughtful analysis to determine whether selling is the wisest move. When investors engage in panic selling, the result may be a self-fulfilling prophecy: The widespread sale of a stock does usually lead to a decline in price. Panic selling is often associated with market crashes, notably the crash that kicked off the Great Depression in 1929, and 1987's infamous one-day crash known as Black Monday.

Risk-On/Risk-Off

In investing, certain assets, such as stocks, are considered to carry more risk than others, such as gold. During periods of market turmoil, some investors may adopt a "risk-off" strategy, meaning they sell their riskier assets to buy less risky ones. Under a "risk-on" strategy, the converse is true: Investors buy riskier assets while selling less risky ones. For example, when investors feel the market is strong and rising, they might perceive less risk about the market and its outlook, creating a risk-on environment. Alternatively, market factors that indicate a market downturn and increased risk may bring about a risk-off environment.

Safe Haven

The term safe haven may make grammarians cringe — a haven, after all, is by definition a safe place, and so "safe haven" is redundant — but that hasn't stopped brokers and investors from employing the term, especially when markets go south. Investments are described as safe havens when it's commonly believed they won't lose value in the face of market turmoil, or, in other words, the investments some might turn to when pursuing a "risk off" strategy. Exactly what types of securities and other investments are considered as safe havens can vary over time — past examples have included U.S. Treasury bonds, the Japanese yen and gold. But sometimes experts disagree as to whether a certain investment should be considered a safe haven or not. Ultimately, it's important for investors to remember that no investment is guaranteed to be "safe."

Sell-Off

On Wall Street, when the going gets tough, many start selling. A sell-off describes what happens when, following a major decline in the prices of stocks, bonds, or other securities, market participants collectively sell massive quantities of those falling securities as each participant seeks to prevent losses from future price declines.

Volatility

When a security, a commodity or an index fluctuates wildly in a short period of time, they're experiencing volatility. The Chicago Board Options Exchange's Volatility Index (VIX) measures the expected volatility of U.S. stocks by gauging investors' expectations of major market moves. Financial market regulations include buffers to limit volatility.

FINRA is the largest independent regulator for all securities firms doing business in the U.S. Its chief role is to protect investors by maintaining the fairness of the U.S. capital market.

FINANCIAL PLANNER

Continued from Page 11

as the events of this year have brought home. Thus, it's crucial that you choose wisely when selecting a trustee and an attorney-in-fact, as they will be entrusted with navigating the future on your behalf. With careful estate planning, and dependable decision-makers ready to act on your behalf, you can assure that your wishes and needs will be met even if you cannot make the decisions yourself.

Alexandra Armstrong is a CERTIFIED FINANCIAL PLANNER professional and Chartered Retirement Planning Counselor and founder and Chairman Emeritus of Armstrong, Fleming & Moore, Inc. Christopher Rivers, a CERTIFIED FINANCIAL PLANNER professional and Chartered Retirement Planning Counselor and co-author of this article is a principal of Armstrong, Fleming & Moore, Inc., Located at 1800 M St. NW, Suite 1010-S, Washington, D.C. 20036-5813, 202/887-8135.