

DISABILITY ALERT



DISABILITY ALERT is a commentary on topics of current interest – usually topics relating to planning for individuals with disabilities and changes to current tax and social assistance legislation. Professional advice should be obtained before acting on any of this information.

LIFETIME FINANCIAL PLANNING FOR INDIVIDUALS WITH DISABILITIES

Many families are confronted with the daunting task of assisting a family member with disabilities with the cost of living. An *individual with disabilities* is someone with significant disabilities because of a mental or physical impairment that will continue. Consequently, the person is substantially restricted in his or her daily living to attend to personal care, function in the community or participate in the workplace. If the impairment is a mental condition things get even more complicated because the person may not be able to own property, sign a contract, have a bank account, own an RRSP or write a will. These issues all cause difficulty in structuring their finances which usually means that financial transactions must be carried out by a family member in their own right on behalf of the individual with disabilities or through a formal trust arrangement. A trust will almost certainly come into play as time marches on.

Funding the lifelong finances of an individual with disabilities is a huge undertaking. It requires a plan not only to manage day to day finances but at the same point must consider the bigger picture to assure continuing availability of funds as parents grow older. Then of course there must be a structure that continues after parents die. Exhibit A attached shows the major inputs of lifetime funding and how they are deployed to cover both current expenses and lifetime needs. It looks complicated so take some time to study it.

Lifetime Funding Alternatives

An Absolute Discretionary Trust, sometimes referred to as a Henson Trust, is a pivotal structure in funding the cost of living of an individual with disabilities. It may allow the individual to qualify for social assistance (in some but not all provinces) and means that a pool of funds will be held by trustees to take care of financial needs on an ongoing basis – subject to the terms of the trust. Starting in 2008, the federal government implemented the Registered Disability Savings Plans (RDSP) which most certainly will become a major block in financial planning for individuals with disabilities. In some cases it may replace the Absolute Discretionary Trust but most likely it will be used in conjunction with a trust. There is a *Tax Alert* on Registered Disability Savings Plans on our website at www.personalwealthstrategies.net. The Absolute Discretionary Trust is shown on the top left part of Exhibit A and the RDSP is shown near the middle on the right side of Exhibit A.

Families who must plan for someone with disabilities must understand the bigger picture of lifetime financial planning. Most often that just doesn't happen and we professionals are not as much help as we should be. It's fine to know about tax credits, trusts, social assistance but how do they all fit together into a financial plan? That's the ingredient that is most often missing. One size planning does not fit all. The purpose of this article is to help you map out that bigger picture.

Cost of Living

It is critical to get a good handle on what is the current and projected cost of living. Otherwise these costs will be underfunded and perhaps even vastly over funded. For this reason you need to know the costs today and how they will change over time. For example, the individual with disabilities may be living with mom and dad but at some point they may move to independent living or assisted living and both will involve a new cost – set out below are the major cost of living categories:

- | | |
|------------------|-----------------------|
| ◆ Housing | ◆ Transportation |
| ◆ Household | ◆ Financial and legal |
| ◆ Personal | ◆ Recreation |
| ◆ Medical | ◆ Other |
| ◆ Attendant care | |

Holding on to Social Assistance

Some families must rely on social assistance simply because they do not have the wherewithal to pay the living costs of the individual with disabilities – either now or in the future. Social assistance in Ontario (under the Ontario Disability Support Program) and in most other provinces only provides financial support to recipients with nominal assets and income – so disability planning needs to be done to keep social assistance in play together with other strategies to move income beyond a subsistence level.

Assume that an individual with disabilities qualifies for \$1,200 a month in social assistance plus drug and dental coverage of another \$500 a month– a total of about \$20,000 a year. Because social assistance is not taxable, the family would need a pretax income of around \$25,000 to provide the same funding. In many cases that is just not possible so it is important that social assistance be built into lifetime financial planning if at all possible.

Tax Credits – A Long Term Funding Source

There are many tax credits available to an individual with disabilities or to a family member who supports that person. Effectively, tax credits can supply cash for day to day expenses or be used to fund long term savings – say a RDSP contribution. If for example, the Disability Tax Credit refund of \$1,500 a year were contributed to a RDSP for twenty years, the individual with disabilities would accumulate about \$200,000 in the RDSP without affecting social assistance programs. Investing the same funds outside a RDSP would only accumulate \$50,000 and probably reduce social assistance entitlements. It costs nothing to get the credits other than applying them.

Following are some of the tax credits and the approximate tax refunds they will generate but the amount will vary from province to province.

Wholly Dependent Credit (single parent)	\$2,020
Disability Tax Credit	1,510
Caregiver Credit	880
Infirm Dependent Credit	880
Medical expenses of dependent –	20% of medical expense

Tax credits as a source of tax free income are shown at the top of Exhibit A.

Annuities

In some cases, individuals with disabilities can only handle personal finances to a limited extent or maybe not at all. Leaving such people with a large amount of money will just not work. Maybe there is no one to administer a trust for the individual with disabilities so what do we do? For individuals with minimal disabilities, an annuity may be the only practical way to help them with their finances. The annuity is shown near the top of Exhibit A.

Funding Sources for a Person With Disabilities

The main sources of long funding for an individual with disabilities (as depicted in Exhibit A) are as follows:

- ◆ Family gifts and bequests
- ◆ Insurance
- ◆ Henson trusts
- ◆ Annuities
- ◆ RRSP proceeds (including inheritances on death of a parent or grandparent)
- ◆ Registered Disability Savings Plans
- ◆ Social Assistance (may opt out for better quality living)

These seven sources must work together in a coordinated fashion both in the long term and the short term. That's what long term planning is all about.

Gifts, Bequests and Tax Planning

Gifts and bequests in one way or another are the pivotal source of family assistance for an individual with disabilities. Funds can be transferred to the person in a number of ways as shown in Exhibit A. The problem is to pick the best route in each particular situation. Good planning can also garner a significant amount of tax free money. Getting to this level is a challenging process and usually can only happen effectively if a lifetime financial plan is part of the process.

You Need a Financial Plan

Planning for an individual with disabilities is no different than long range financial planning for the rest of the family. There needs to be a plan – otherwise the financial future of the individual is left to chance. We are in the process of developing a comprehensive cash flow projection to support such plans which we believe will be helpful. However, you need to address the following issues before that can start:

- ◆ Is there enough money to last for the life of the individual with disabilities _____
- ◆ If funds are insufficient, should insurance be purchased and if so how much _____
- ◆ How do we maximize the benefits of a RDSP over simply investing the funds _____
- ◆ Is cash flow arranged so that social assistance is not lost _____
- ◆ Are we taking advantage of all tax credits and other incentives _____
- ◆ Are there appropriate discretionary structures in place to meet unexpected changes in the financial requirements of the individual with disabilities _____
- ◆ Is the supporting documentation such as wills and trusts up to date and compatible with the financial plan _____
- ◆ Have we dealt fairly with siblings and other members of the family _____
- ◆ Have we had a family conversation to get buy in from everyone _____

Long term financial planning is essential. It will take a while to work it out and it may be a frustrating process but it must be done. There are plenty of advisors with their own specialties but you must also find ones who can help you understand the big picture. Start to put some of the building blocks in place now and you will eventually get there.

This article was originally published in the Canadian MoneySaver magazine but has since been amended.

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LIFETIME FUNDING FOR AN INDIVIDUAL WITH DISABILITIES

EXHIBIT A

