Disabilities, special needs and financial planning (Large print edition*)
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Transferred amounts .............................................. 17
Coordinate your private planning options ................. 18

The new RDSPs .......................................................... 19
Overview of RDSPs ..................................................... 19
Who may benefit from an RDSP? ............................... 20
One-to-one relationship .......................................... 20
Contributions ........................................................... 21
Canada Disability Savings Grant (CDSG) ...................... 21
Canada Disability Savings Bonds (CDSB) ..................... 22
Payments ............................................................... 22
Assistance holdback amount ...................................... 23
Effect on income-tested government benefits .............. 23

Henson trusts .......................................................... 25
The story of Leonard and Audrey Henson ................. 25
A passing grade ....................................................... 26
A Henson trust "with distinction" ................................. 28

Insurance and children ............................................ 30
Young families ....................................................... 30
Riders ..................................................................... 31
RESPs displace universal life ..................................... 31
Permanent needs ................................................... 32

Contact us ................................................................ 34
Summary: Disabilities, special needs and financial planning  By ADVISOR Staff

(May 2008) A surprising number of people have a significant financial planning challenge weighing heavily on their minds, one that has very little to do with retiring debt-free or travel to Florida — they're concerned about planning for the ongoing care of dependent, special needs adult children.

The statistics suggest nearly every advisor has at least one family in their book of business who has this concern. That number is even higher when you take siblings, friends, extended family members and other caregivers into account.

Planning for special needs, page 6.
When your dependent child faces a lifetime of inherent disability-related earning limitations and continued dependency into adulthood, perhaps for many years after you're no longer around to care for them, an advisor's standard talk about retirement planning is likely going to fall short of the mark. By Kate McCaffery, Advisor.ca.

Financial and tax supports for persons with disabilities, page 12.
People with physical and mental disabilities often face serious financial challenges related to earning limitations or direct out-of-pocket expenses. It can be a dizzying journey to understand the value and interaction of tax measures and financial assistance designed for persons with disabilities, and families generally need to take coordinated financial and estate planning steps to optimize those public sources. To get started, it helps to understand what options are available. By Doug Carroll, AIM Trimark Investments.
The new RDSPs, page 19. Registered Disability Savings Plans (RDSPs) were first proposed in the March 2007 federal budget, they were set to be available for the first time in 2008, and yet nearly halfway through the year you still can't open one for a disabled beneficiary. So what's the holdup? By Jamie Golombek, AIM Trimark Investments.

Henson trusts, page 25. If you are disabled, an inheritance can hurt you or help you. It depends on how things are structured. By John Poyser, Inkster, Christie, Hughes LLP.

Insurance and children, page 30. An insurance policy is no substitute for the help and affection a child loses when a parent dies, but it can eliminate debts and provide needed financial support by replacing the income he or she might depend on. For mothers and fathers who want to protect their children from financial hardship, there are different life insurance policies, options and specific strategies to consider. By Andrew Rickard, special to Advisor.ca.
(May 2008) When your dependent child faces a lifetime of inherent disability-related earning limitations and continued dependency into adulthood, perhaps for many years after you're no longer around to care for them, an advisor's usual talk about retirement planning is likely going to fall short of the mark.

Statistically, there is a very good chance your client list includes at least one, if not several people who would agree with this statement; who have the care of a dependent, special-needs family member high on their list of concerns or priorities, and for whom your standard retirement planning regimen simply will not cut it.

What's more, those who specialize in the type of planning these families need say the group is often underserved by tax advisors and lawyers who are not always aware of the opportunities available or the financial consequences of seemingly minor asset-planning or tax-filing missteps.

**The statistics**

According to the *Participation and Activity Limitation Survey* conducted by Statistics Canada, roughly 3.7% or an estimated 202,350 children under the age of 14 in Canada had a reported disability of some kind. For children between ages five and 14, reported disabilities were severe and very severe for 23.5% and 18.9% of those surveyed.

Although the numbers are small, at a glance, Ken Pope, an Ottawa-based lawyer who specializes in assisting families with children who have special needs, points out that each of those 200,000+ children have family units consisting of parents, siblings and more, who are likely all concerned...
about the child's care and welfare. As well, in addition to the statistics related to children, in Ontario alone, more than 309,155 adults between 18 and 65 currently receive disability benefits under the Ontario Disability Support Program (ODSP).

"Statistically it works out to be, at the minimum, one family in 10 that is either a parent household or a sibling household. If you go into any room of 100 people, and I know from doing this, you're going to find 10 people who are the parents of, or the brother or sister of a child with disabilities. It's huge," he says. "In fact, one in eight is the real figure. I don't think anybody has a proper understanding of the size, the immense number of families who have this as a concern."

Helping clients to recoup unclaimed tax credits and establishing trusts that disabled heirs can inherit without negatively impacting income-tested government benefits make up a large part of Pope's practice. On average, he says he's able to recapture between $13,000 and $18,000 for clients by backfiling for the three-year statutory period allowed by the CRA, plus another seven years under the Fairness Package, legislation that allows the CRA to use discretion and reassess income tax returns beyond the normal three-year period under certain circumstances.

The problem cases come to him when accountants have never claimed or backfiled for disability or caregiver credits on behalf of the family. "Maybe the client doesn't offer that they have a family member with disabilities, but the clients who are most ticked off are the ones where they have accountants who've done work for them for many years, and they've just never told [the family] about the credits," says Pope.

"Advisors should ask the family — do you have a child with special needs? And then go from there in the know-your-
client sense. Until you've dealt with this one, you can give the clients all the advice you want. Retiring happily and all this stuff, it's not their core concern. Their core concern is what happens if I die tomorrow? What will happen to my child? From a financial advisor and an estate planner's perspective, that's the issue."

**Tax planning**¹

Claiming disability and caregiver credits can be an onerous and complicated task. When asking those clients who do qualify for the support whether or not they are using the credit, Pope says roughly 45% say no or that they're unsure — a reasonably good sign that they're not using the credits since the filing process, which requires input from doctors and approval by the CRA, is difficult to miss or forget.

He also says a lot of people walk away from claiming the credits because the process is complicated, and the onus is on the disabled person filing the paperwork, to prove they qualify.

Pope says it helps to ask about the nature of the disability, whether or not the child is on ODSP or similar if they're over the age of 18, and how much they receive each month, along with whether or not clients are using the disability and caregiver credits.

"The most common recapture is $13,000 for the disability if the child is, say, as old as 28 and living with the parents, plus another $6,000 for the caregiver credit. If the child is 18 or under, there is a further substantial recapture for the child disability tax credit supplement, on top of the disability

¹ For more about tax planning and the credits available to your clients, read *The new RDSPs*, by Jamie Golombek; page 19. Also, *Financial and tax supports for persons with disabilities*, by Doug Carroll; page 12.
tax credit," he says. "The recapture on that can easily be $24,000 in total."

In claiming ODSP, he says "there's a right amount and a wrong amount" clients should be receiving. Many times recipients are automatically given lower amounts, based on their circumstances — an adult child living at home with a parent who makes the meals can receive $762 in Ontario for room and board. If a lease is set up between the parent and the child, however, and the child contributes to the shelter costs in the home, that number is increased to $999.

**Trusts**

Proper trust planning is perhaps the biggest and most important part of estate planning that is intended to leave assets behind for the well-being and benefit of disabled heirs.

Unfortunately, having assets, even the proceeds from an insurance policy, will cause trouble for beneficiaries who are dependent on income-tested benefits. Trusts can be established, but must include very specific wording to keep from impacting government assistance payments.

Henson trusts include a non-vesting clause that should make it clear that the trust beneficiary does not own the assets, the funds are held in trust, to be distributed at the sole discretion of named trustees. Other trusts holding assets under $100,000 can also be established under certain circumstances.²

For advisors, the date a client last updated his or her will could be an interesting flag for consideration when talking about whether or not their will includes a proper Henson trust. Although the Henson case settled in 1989, observers

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² For more, read *Henson trusts*, by John Poyser; page 25.
say most wills drafted before 1996 likely do not have a proper trust in place. Pope says it's usually the case that wills established after 1996 sometimes include a basic Henson trust with core elements, but that many are still worded incorrectly.

"One of the most common precedent minders for lawyers is section six of O'Brien's Wills and Trusts, Division V. When a lawyer doesn't quite know what to do for a precedent in a will, he goes to O'Brien's, in this case to look up Henson trust. Until a few years ago it was just one small section at the back. They send updates twice a year to stuff into the three-ring binder. I think it's been corrected, but keep in mind that not everybody gets these annual updates, right?"

Until recently, he says the two sections which referred to Henson trusts did not include or discuss key non-vesting provisions because they weren't pertinent to the references (encroachment on capital) where the trusts were mentioned.

"This is the most common flaw — the missing non-vesting clause," he says. "Of the wills that have a trust of some sort, and the bulk don't, maybe one is correct, one is half correct and the third is wrong, which in some cases is worse than nothing."

**Insurance**

By all accounts, insurance is an easy sell in this sort of planning — T100 is recommended for its relative affordability and fixed premiums. Joint and last insurance where premiums cease after the first parent's death are also appealing.

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For more insurance planning options, read *Insurance and children*, by Andrew Rickard; page 30.
To save $100 each month in an effort to accumulate $200,000 to benefit heirs, clients would need to save for 2,000 months or 166 years. By comparison, $100 a month in set premiums is a far more attractive option for clients.

The trick, however, is getting the insurance properly designated to the beneficiary's Henson trust. Back offices are used to setting up policies where beneficiaries receive payouts "in trust," a bare interest account, but are usually not versed in setting things up for beneficiaries to receive funds in trust, pursuant to the terms of a Henson trust in a will.

Pope says he's run across insurance companies who would only set things up properly if the designations were typed on the company's letterhead. In another quirky example, the company in question would only make the proper designations if the client's wills were probated within six months of death — an unreasonable condition that was quickly remedied when pointed out.

"This is the stuff that I do not want to find out when the client is dead," he says. "You really need to have enough experience that you don't have all of this stuff bite you when somebody dies."

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Financial and tax supports for persons with disabilities
By Doug Carroll

(May 2008) People with physical and mental disabilities often face serious financial challenges related to inherent earning limitations or direct out-of-pocket expenses.

Fortunately, government support is available, but it can be a dizzying journey to understand the type, value and interaction of tax measures and direct financial assistance designed to assist persons with disabilities. As well, the disabled individuals and their families generally need to take coordinated financial and estate planning steps to optimize those public sources.

To get started, it helps to understand what direct financial assistance and relieving tax measures are available.

Direct financial assistance

Canada Pension Plan / Quebec Pension Plan
The CPP/QPP disability benefit is available to people who have made recent CPP/QPP premium payments while they worked. The disability must be both:

- Severe, where a person is incapable of regularly pursuing any substantially gainful occupation; and

- Prolonged — the disability will prevent a return to work at any job in the next 12 months, or is likely to result in death.

The maximum monthly disability benefit a qualifying disabled person can receive in 2008 is $1,077, plus a maximum monthly benefit of $208 for each dependent child of a disabled contributor. These are related but separate
applications that must be made using forms available through Service Canada.

Child disability benefit
Based on family net income, the federal government will pay as much as $195 per child each month to families with children qualifying for the disability amount (see below). Tax form T2201 must be completed and approved by the CRA in order to qualify, and the payment is then delivered as part of the monthly Canada Child Tax Benefit payment.

Provincial support programs
Some provinces have stand-alone disability support programs, while others recognize disability as a special qualification within the overall social support system. Generally though, for participation or qualification, the disability must be certified by a licensed physician using provincially prescribed criteria and forms.

Entitlement is reduced or eliminated where earnings or assets exceed regulated thresholds. In some provinces it may be possible to set up a discretionary trust (sometimes called a "Henson trust" for the Ontario case first litigated on the issue) to keep assets available for the person's benefit but outside of this calculation. (See the link at the end of this article for more on Henson trusts.)

The composition of service offerings, cost reimbursements and direct financial assistance varies considerably from province to province. The maximum annual, direct financial assistance disabled persons receive from provinces, on average, comes in just under $10,000.
Individual income tax relief

Tax measures commonly available to assist persons with disabilities generally fall into three categories. These include:

- Deductions: Qualifying items reduce the taxable income upon which relevant federal and provincial tax rates are applied to arrive at initial tax liability.

- Non-refundable tax credits: Once tax liability is calculated, these credits directly reduce that liability but cannot take it below zero. The qualifying amount is multiplied by the applicable federal or provincial rate (usually the lowest bracket rate) to arrive at the credit value. For 2007 reporting, the federal rate is 15%.

- Refundable tax credits: These may result in an amount payable to the individual even where tax liability has been reduced to zero.

Focusing on the 2007 tax reporting year, the following is a bit of a road map that identifies key items, and attempts to put them in context with one another.

Disability amount
This is a non-refundable credit, available both federally and provincially. Using tax form T2201, the disability must be certified by a qualified medical practitioner as being both severe and prolonged.

- Severe: Blindness, conditions requiring life-sustaining therapy, a marked restriction in speaking or hearing, walking, feeding, dressing, elimination or a marked restriction in everyday mental functions.

- Prolonged: Lasting, or expected to last, continuously for at least 12 months.
The basic federal amount is $6,890, with a supplement worth as much as $4,019 if the disabled person is under age 18. Taken together, the maximum possible federal credit is $1,636.

The maximum basic credit range at the provincial level ranges between $386 and $758.

Disability supports deduction
A disabled individual may deduct qualifying, out-of-pocket expenses incurred to work, go to school, or conduct grant-supported research. The individual may not deduct amounts already claimed under the medical expense credit (whether claimed by the individual personally or on his or her behalf as a dependant), or amounts already reimbursed by health insurance plans or through other non-taxable payments.

The deduction cannot exceed the person's earned income for the year, which generally includes:

- employment income and net self-employment income;
- the taxable part of scholarships, bursaries, fellowships, and similar awards;
- net research grants, and
- earnings supplements and financial supports under most government-sponsored employment programs.

For students at designated institutions, however, the deduction may be as much as $15,000 more than their earned income.

Medical expenses
An individual may claim eligible medical expenses paid, whether incurred in Canada or elsewhere, in any 12-month
period. Special rules apply to attendant care expenses, whether the care was received at home or in an establishment. Eligible amounts can be claimed as a medical expense, or as a disability support deduction.

This is a non-refundable tax credit, equal to expenses that exceed the lesser of:

- $1,926, or
- 3% of the disabled individual's net income.

This number ranges between $1,620 and $1,936 in different provincial formulas.

As indicated above, it is not possible to claim both the supports deduction and the medical expense credit for the same cost. Accordingly, a test calculation should be run to determine which of the two yields the best net tax result.

Refundable medical expense supplement

This is a refundable credit designed to assist people with very low incomes who claim either the disability supports deduction or the medical expense credit. Subject to a clawback where family net income exceeds $22,627, this federal credit can be worth as much as $1,022.

Income tax relief for dependants

Caregiver amount

This non-refundable credit is designed for individuals providing in-home care to an immediate family member or certain close relatives. If this credit is claimed by anyone, the infirm dependant 18 or older credit (which is of equal value) may not be claimed. Furthermore, this credit is reduced when the eligible dependant credit is claimed for the same live-in person. The federal credit is worth $623; provincial credits range from $225 to $442.
Child care expenses
The calculation of this credit can be complicated, even without disability issues to consider. For present purposes, be aware that there are provisions to guard against double counting where concurrent claims are made for the disability amount or the medical expense credit.

Children’s fitness tax credit
This is a new non-refundable federal credit, introduced in 2007. For children eligible for the disability amount, this credit may be doubled to be worth as much as $150. The basic fitness tax credit — 15% of $500 spent on eligible expenses — is generally worth $75 to families. For disabled children, the eligible amount parents can claim is doubled to $1,000, making the credit worth $150.

Transferred amounts
An individual may be able to claim certain amounts, notably the disability amount and the medical expense credit, transferred from a spouse, common-law partner or dependant.

GST/HST relief
Many goods and services used by persons with disabilities are not subject to goods and services tax/harmonized sales tax, whether by exemption or rebate. These include:

- Most healthcare services;
- Personal care and supervision programs while a primary caregiver is working;
- Prepared meal delivery programs;
- Public sector recreational programs designed for persons with disabilities;
- Medical devices and supplies.
Coordinate your private planning options

In order to optimize access and use of government financial and tax supports, individuals and families must conscientiously manage their income and assets. This includes family estate planning, up-to-date wills, beneficiary designations, powers of attorney and the use of different trust structures.⁴

What will be most interesting in the coming years will be to see how these planning activities are affected by the availability of the new registered disability savings plan.

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⁴ For more, read Henson trusts, by John Poyser; page 25.
The new RDSPs
By Jamie Golombek

(May 2008) Registered Disability Savings Plans (RDSPs) were first proposed in the March 2007 federal budget, they were set to be available for the first time in 2008, and yet nearly halfway through the year you still can't open one for a disabled beneficiary. So what's the holdup?

It's not the legislation itself, which was actually passed into law late last year, but rather the enormous complexity financial institutions and Human Resources and Social Development Canada (HRSDC) face when establishing the plans, the infrastructure and systems programming that will be needed to track not only contributions, but the government bonds and grants as well.

That said, it's only a matter of time before the first RDSP is established in Canada, hopefully by the end of 2008.

Once these plans are established and available, they will prove to be a very useful tool to encourage long-term savings by and for persons with disabilities.

Overview of RDSPs

An RDSP is a registered investment plan under the Income Tax Act, largely modelled after the Registered Education Savings Plan (RESP) and the associated grant and bond incentive programs, but there are some significant differences.

As with RESPs, money contributed to an RDSP is not tax-deductible. Government grants and bonds are deposited directly into the plan. Such grants to the plan can be as much as 300% of contributions, and bonds can even be
obtained without making any contributions, as long as a "net income" test, discussed below, is satisfied.

Earnings and growth on all deposits accrue on a tax-deferred basis. The disabled beneficiary is the only person entitled to any payments. The beneficiary is taxed on the earnings and growth when payments are received from the plan. Contributions are not deductible and therefore not taxed in the beneficiary's hands.

As well, there are absolutely no restrictions placed on the use of RDSP payments, as long as they are either received by the beneficiary or applied for his or her benefit.

**Who may benefit from an RDSP?**

In order to open a disability savings plan, the beneficiary of the plan must qualify for the disability tax credit (DTC) in the year of establishment. As long as the person continues to be a DTC-eligible individual, the plan may continue to receive deposits, shelter growth and earnings from taxation, and eventually distribute the accumulated funds to the plan beneficiary.

**One-to-one relationship**

There is an absolute one-to-one relationship between a plan and a beneficiary — each plan can have only one beneficiary and each individual can have only one plan at any given time. This differs from other plans such as RRSPs, RRIFs and RESPs where you can open multiple plans, provided you stick to contribution limits across all plans.
Contributions

Contributions to a plan are not tax-deductible. There are no annual limits but there is a lifetime limit of $200,000 of total contributions (excluding grants, bonds and growth). Contributions can be made in a given year provided that the beneficiary is eligible for the DTC.

Unlike RESPs where the subscriber is entitled to a tax-free return of his or her contributions, once RDSP contributions have been made to a plan, those funds can only be paid out for the benefit of the disabled beneficiary.

Canada Disability Savings Grant (CDSG)

The CDSG encourages the use of an RDSP by matching up to 300% of annual contributions made into a plan, to a lifetime maximum of $70,000. Qualification for a grant is determined by measuring "net family income" (defined below) against a threshold level.

Where net family income is below the threshold level, $75,770 in 2008, the government will provide:

- $3 for every $1 on the first $500 of contributions, plus
- $2 for every $1 on the next $1,000 of contributions.

Where net family income exceeds the threshold, the government will provide:

- $1 for every $1 on the first $1,000 of contributions.

"Net family income" is determined by considering the age and spousal status of the beneficiary. For a beneficiary under 19, it is the combined net income of that person's parents. For a beneficiary 19 or older, it's the disabled beneficiary's own family "net income."
Grants are available for contributions made up until the end of the year in which the beneficiary turns 49.

**Canada Disability Savings Bonds (CDSB)**

The CDSB is targeted to support low- and modest-income families, children in care, and adults without family support.

CDSB entitlement is not dependent on contributions. It provides up to $1,000 per year to RDSPs, up to a maximum lifetime limit of $20,000 per disabled beneficiary.

The maximum annual amount of CDSB assistance of $1,000 will be paid to an RDSP where family net income is below $21,229 (2008) and will be phased out fully at income above $37,884 (2008).

**Payments**

There are two types of RDSP payments:

- *Lifetime* disability assistance payments (LDAP) and
- Disability assistance payments (DAP).

Lifetime disability assistance payments or LDAPs must commence no later than the year in which the beneficiary turns 60 years of age. The total of all LDAP payments in a calendar year is subject to a maximum as follows:

\[
\frac{\text{Fair market value of the RDSP}}{[(\text{Greater of 80 or Age}) + 3] - \text{Age}}
\]

Whether a plan is allowed to make the more general "disability assistance payment" or DAP must be specified in the particular plan documentation at outset or in later amendments to plan documentation. Such payments,
random lump sum payments that can be withdrawn prior to age 60, can give the beneficiary more flexibility. These are not subject to any age constraints but a DAP will not generally be allowed if accumulated government assistance has been greater than personal contributions.

Although plans can allow both payment types, beneficiaries will be required to withdraw LDAPs. In a given calendar year, if the total of all past bonds and grants paid exceeds the total of all past contributions made, a minimum payment equal to the LDAP maximum formula above must be taken each year once the beneficiary reaches age 60.

Each RDSP payment is a blended return of contributions (non-taxable since the contributions were made using after-tax dollars) and grants, bonds, and earnings on all deposits (taxable), making each payment dollar partially taxable.

**Assistance holdback amount**

In the event an RDSP is terminated by the holder, the beneficiary ceases to be eligible for the DTC, the beneficiary dies or a DAP is paid, any grants or bonds received in the ten years prior must be repaid This amount is called the "assistance holdback amount." Note, however, that earnings and growth on the amount need not be repaid. If the beneficiary dies, the contributions and earnings (less the holdback) belong to the beneficiary's estate.

**Effect on income-tested government benefits**

The last remaining issue to be resolved before these plans begin to become widely accepted is whether a disabled beneficiary who has accumulated assets in an RDSP or who begins to receive DAPs or LDAPs will be disqualified from receiving government disability benefits that are based on an asset or income test.
The federal government has already taken the lead on this by amending the Income Tax Act to ensure that RDSP income will not affect the disabled beneficiary's entitlement to the GST credit, the Canada Child Tax Benefit or Old Age Security payments.

As of the time of this writing, only British Columbia and Newfoundland have explicitly stated that RDSP assets and income will not affect provincial income-tested disability entitlements. Will other provinces follow? It remains to be seen.

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Henson trusts
By John Poyser

(May 2008) If you are disabled, an inheritance can hurt you or help you. It depends on how things are structured.

The story of Leonard and Audrey Henson

Leonard Henson had a daughter named Audrey. She was mentally disabled. The Ontario government provided her with a monthly cheque as income support. It also provided her with government programming that was critically important to preserving her lifestyle. All appeared to be well. Leonard could visit her, and used his own money wherever necessary to make sure she had the little extras that made her happy and comfortable. But trouble was brewing.

Leonard was getting older. He wanted to leave an inheritance to Audrey, but knew that the government of Ontario was going to cut off her income support and some of her programming if she inherited any wealth from him. The income support and programming was only available to recipients who were financially eligible. Audrey would not be eligible if she had a few hundred thousand dollars in the bank.

Leonard Henson and his lawyers drafted a specialized last will and testament. It established a trust to hold Audrey's inheritance. Her money would be held on her behalf by trustees appointed under the will. They would spend the money for her benefit, buying her the extras that her father always had, but Audrey would never legally be able to demand any of the money. The decision to give her money from the trust was exclusively at the discretion of the trustees who would only give her money if it improved her lifestyle. They would not give her money if there were any chance it would disqualify her from government support.
When the will was well drafted, Leonard must have loved it. When he died, though, the government of Ontario was less impressed. They cut Audrey off, discontinuing her income support. Effectively, they told the trustees to support her out of the trust until the whole of the inheritance was gone, at which time she would then be eligible to reapply for income support.

The trustees decided to fight the government. The case wound its way through administrative tribunals and courts all the way up to the Ontario Court of Appeal. The trustees won: The court said a disabled person like Audrey could inherit under a fully discretionary trust and still remain eligible for government support and programming.

The wheels of justice grind slowly though, and the legal dispute lasted for years. Audrey died before the final ruling.

A fully discretionary trust for a disabled person has come to be called a "Henson trust." These trusts are now a mainstay in estate planning for disabled heirs across Canada. The exception is Alberta, where the rules were changed in 1999 to make these trusts ineffective.

In the past 20 years that Henson trusts have been on the legal landscape, we have learned some lawyers do a good job drafting a Henson trust and others don't. A financial advisor can help a client by recommending the use of a Henson trust, but also by knowing enough to make sure the client is getting exactly what the family needs.

**A passing grade**

At the core of a Henson trust is the language which makes it clear that the income and capital in the trust is to be parcelled out for the benefit of the disabled heir, *only* when the trustees decide to do it.
If you find any language in the trust that discusses mandatory payments or would allow the beneficiary to demand any payment or distribution from the trust, then it fails as a Henson trust.

Consider a clause, for example, that provides that "the trustees shall pay a monthly allowance to my disabled child equal to half of the income earned by the trust in each year." That language would put the trust offside. Why? If the trustees withheld payment of the allowance, payment could be forced by a court.

The published decision of the Ontario court in Henson quoted the language from Leonard Henson's will at some length. Any lawyer drafting a Henson trust would be well advised to simply cut and paste the same language into the will he or she is drafting. Look for this language or language much like it:

No Vested Interest — No interest in the capital of the trust or in the income thereon, or any portion of either, shall vest in [beneficiary name]. His interest shall be limited to any sums paid to him or paid on his behalf.

**Going from a passing grade to an "A"

These are the basics, but after 20 years of drafting Henson trusts, many lawyers are now going beyond just the basics.

A well-drafted Henson trust is built to stand the test of time, since it might be in place for several decades. Trustees selected by the client may not survive the disabled heir. Thus, the trust should allow for replacement trustees to be appointed when initial trustees are getting long in the tooth.

A well-drafted Henson trust should be flexible. The trust might contain clauses allowing the trustees to wind up the trust if it no longer serves its purpose. At windup, the trustees might have the option to purchase an annuity for
the disabled heir, or even to give the money to them directly where that makes sense. The trustees might like a provision expressly allowing them the chance to appoint a trust company and resign.

A well-drafted Henson trust will contain language making it clear that the trustees can spend money freely on the disabled beneficiary, without any regard for how much money might remain in the pot for the subsequent generation of beneficiaries after his or her death. Otherwise, an "even-hand rule" may operate to force a legal balancing act between the disabled heir and future beneficiaries.

**A Henson trust "with distinction"**

Changes to the *Income Tax Act* have been announced that will allow for the tax-free rollover of registered investments into a trust for a disabled family member. This allows for the deferral of taxes that would otherwise be triggered at death. To qualify, the trust will have to meet requirements of the soon-to-be enacted section 60.011 of the Act, which describes a trust where income and capital are to be used for the "comfort, care and maintenance" of the disabled beneficiary. If that rollover is to be secured, the trust should contain clauses using the same language to create a close link between the trust and the language permitting the rollover.

At the technical forefront, some Henson trusts are drafted to sidestep the difficulties that arise in Ontario because of the "rule against accumulations." This trust rule, not a tax rule, provides that income earned by a trust in Ontario can be kept in the trust for the first 21 years only. In the 22nd year of the trust's existence, all income earned on trust assets must be paid out each year.

If the income is paid out to satisfy this accumulation rule and the beneficiary of the trust is disabled, the mandatory
payment of income to them would make them ineligible for government support. Thus, draftspeople in Ontario usually include a clause to include a pool of income beneficiaries, one of whom is the disabled heir, and provide that the mandatory income stream be directed among the pool on a discretionary basis.

That solves the accumulation problem, but can be an unpalatable solution for other reasons. The client usually wants the money to benefit the disabled family member — an income clause spreading the income among others is generally contrary to the client's wishes. The client may want the trust to grow. Growing the trust becomes difficult when all of the income needs to be distributed. Reinvesting it allows for faster growth.

Is there a better solution? The trust can be structured in a way to be governed by the laws of a province other than Ontario. To achieve that, the trust is best set up while the parent is alive, should not contain land and should be administered by trustees resident in the other province. It should also contain a clause expressly choosing the accumulations law of the other province as intended to govern the trust.

A basic Henson trust is a necessity for most families with a disabled beneficiary. The better the Henson trust, the better the outcome for the disabled heir.

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Insurance and children
By Andrew Rickard

(May 2008) An insurance policy is no substitute for the help and affection a child loses when a parent dies, but it can eliminate debts and provide needed financial support by replacing the income he or she might depend on. For mothers and fathers who want to protect their children from financial hardship, there are different life insurance policies, options and specific strategies to consider.

According to Statistics Canada's most recent Survey of Financial Security, the median debt load for Canadians increased by 38% between 1999 and 2005, driven primarily by rising real estate prices and larger mortgages. Households in which the major income recipient was under the age of 35 owed the most of any demographic, holding $39.40 worth of debt for every $100 they had in assets.

Young families

For families like this, term insurance is the obvious choice because it provides the largest amount of protection for the least amount of money. Indeed, when clients are in good health and non-smokers, purchasing an individual term insurance policy to cover a mortgage can even be cheaper than taking the creditor group insurance offered by the banks.

But insurance can and should do more than simply eliminate the family’s largest debt. A full capital needs analysis will reveal how much additional coverage is required to replace lost income and fund expenses such as daycare and education.
**Riders**

Most life insurers will also extend coverage to the family's children under the same policy.

Manulife, for example, allows buyers of their Family Term product to add a child protection rider. "It offers low-cost coverage that would pay for a $10,000 death benefit and, more importantly, locks in the child's insurability for when they reach adulthood and need more coverage," says Natasha Krivokapic, product manager for Manulife's individual term insurance products.

On the policy anniversary closest to the child's 25th birthday, when the child either marries or when the child has children of his or her own, the rider can be exercised and used to purchase up to $250,000 of insurance without medical evidence. Krivokapic says it's a popular option with advisors. About 20% of the company's Family Term policies are issued with the child protection rider in place.

Other companies, such as Empire Life and Canada Life, are now offering riders that will pay a lump sum benefit if the insured's child is diagnosed with a critical illness. Others, such as Standard Life, are even marketing individual CI plans specifically for children.

**RESPs displace universal life**

Years ago some advisors recommended taking out a universal life (UL) insurance policy on a child as a means to save for his or her education. Investment growth was sheltered from taxation for as long as funds remained inside the plan, and at age 18 the policy could be transferred without triggering attribution. But when the contribution limits on Registered Education Savings Plans were increased
in 1997, and incentives like the Canada Education Savings Grant were added, the popularity of UL for children began to wane.

"We do not see universal life being used as a vehicle for saving for children's educations," says Marty Mommersteeg, product manager for Manulife's universal life products. "Universal life is being used for juveniles in inter-generational wealth transfer situations. In these cases, wealthy parents or grandparents are purchasing insurance for the children to help the children deal with the tax liabilities their inherited wealth will eventually create."

**Permanent needs**

Universal life may also be appropriate for families with a permanent insurance need, for example, in the case of those who want to provide for a disabled child.

Glenn Stephens, a lawyer who works as a planning consultant with PPI Financial and author of *Estate Planning with Life Insurance*, says that it's difficult to say whether UL or term-to-100 insurance product is used more often in these kinds of circumstances. "But it would be one or the other, and it would be joint last-to-die, assuming both parents are alive and insurable," he says.

He says that universal life appeals to those who want to quick-pay, and put a relatively large amount of money into the policy in a short period of time. He also says some clients like the idea that they can employ leverage, and take out a tax-deductible loan against the cash surrender value of a UL policy to use for investment purposes. Stephens points out that any solution using UL will be driven by cash flow. "If you're looking for the absolute cheapest way to do it, and you're not a high-income type of person, for sure the straight T-100, joint last-to-die would be the best option."
Stephens concludes with a warning against using plain old T-10 or T-20 insurance in circumstances involving children with developmental disabilities. "Because it's a permanent need, term insurance is not the way to go with this," he says, noting that the cost of term insurance will become prohibitive and coverage will eventually lapse if it is not converted to a permanent plan.

"You're dealing with disabled dependants who aren't going to get better. Even if those children are 50 when you die, they're going to need financial support, and they're going to presumably need the insurance at that time," he says.

**Editor's note:** Sudden windfalls of cash — inherited assets, whether they come from insurance policies or direct will bequests — can create significant trouble and sometimes hardship for beneficiaries dependent on income-tested government benefits.

For more on this and for more information about how to structure inheritances so beneficiaries can avoid this trouble, read *Henson trusts*, by John Poyser on page 25.

*Filed by Andrew Rickard.*
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