PLANNING AND ADMINISTRATION OF HENSON TRUSTS

SOME PRACTICE TIPS

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It is now common practice for parents with disabled children to incorporate a Henson trust in their estate plan.

In most cases, the share of the estate allocated for the disabled beneficiary is directed to be held by a trustee in a fully discretionary trust during the disabled child's lifetime. The trust is typically created in the parent's Will. The trustee is given discretion to pay income or capital to the child and income that is not allocated to the child is typically directed to be accumulated in the trust, subject to the provisions of the *Accumulations Act* that require trust income to be distributed after twenty-one years.

The disabled child's share of the estate is set aside in such a trust, both for the purpose of preserving the beneficiary's entitlement to government benefits and to avoid the need to appoint a guardian of property to manage the disabled family member's interest in the estate.

When drafting Henson trusts, it is important to have an understanding of the Ontario Disability Support Program ("ODSP") rules and exemptions.

We will first provide an overview of the ODSP plan and conclude with some Will planning and estate administration tips.

OVERVIEW

1. The ODSP provides income support and related benefits to persons with a disability as defined in the *ODSP Act*.

   If the disabled person is at least eighteen years of age, has not attained the age of sixty-five, his or her income and assets do not exceed the prescribed limits and he or she and their prescribed dependants provide verification of information required to determine eligibility, the disabled person and dependants will be entitled to income and shelter support and coverage for prescription drugs.

   A disabled person living independently, with no dependants, currently receives about $600.00 per month for basic needs and about $480.00 per month for shelter for a total monthly payment of about $1,080.00.

   When the value of drug coverage is also taken into account, the disabled person may receive significant monthly benefits under the government plan.

2. In order to qualify for these benefits, the disabled person must meet an asset and income test. The basic asset limit is $5,000.00 and the basic income limit for the benefit unit (defined as a person and all of his or her dependants on behalf of whom the person receives or applies for income support), in a twelve month period, is $6,000.00.

3. Although the basic asset limit is $5,000.00, some assets are exempt from that limit. A few examples of exempt assets include:

   (a) The disabled person's interest in a principal residence for the benefit unit.

   (b) The value of the disabled person's interest in a motor vehicle.

   (c) Tools of the trade that are essential to the employment of a member of the benefit unit.

   (d) Certain business interests, subject to dollar limits and Director approval.

   (e) A prepaid funeral.

   (f) An amount not exceeding $100,000.00 received as damages for pain and suffering or received as an award of damages under S. 61 of the *Family Law Act*. Amounts over $100,000.00 could also be exempt if the Director of the ODSP is satisfied that such funds will be used to pay for disability related expenses; and

   (g) Up to $100,000.00 of capital derived from an inheritance or life insurance policy that is held in a trust – commonly referred to as a Maintenance or Expense trust.

   The forgoing is a general summary of some of the most common examples of exempt assets. For a full list of exempt assets and additional details refer to S. 28 of Ontario Regulation 222/98 under the *ODSP Act*.

4. Some funds and payments are also not included as income and hence would not violate the $6,000.00 income limit. Examples include:

   (a) The portion of a payment received from the sale or other disposition of an asset that is applied, or if the Director approves, will be applied towards:

      (i) the purchase by a member of the benefit unit of a principal residence used for the benefit unit;

      (ii) the purchase of any other asset that, in the opinion of the Director, is necessary for the health and welfare of a member of the benefit unit;

      (iii) purchase of an asset that is not included as an asset under S. 28.

   (b) Interest earned on that portion of the assets that are within the prescribed asset limits.

   (c) Payments from a trust or from a life insurance policy, gifts or voluntary payments that are applied to:

(i) expenses for disability related items or services for a member of the benefit unit that are approved by the Director and that are not and will not be otherwise reimbursed;

(ii) certain education and training expenses that are approved by the Director;

(iii) certain amounts payable pursuant to a court order for such things as disability related expenses.

(d) Payments from a trust or life insurance policy or gifts or other voluntary payments up to a maximum of $6,000.00 for any twelve month period.

(e) A gift received for the purpose of making a contribution to an RDSP, if the gift is contributed in a timely manner; and

(f) All payments from an exempt RDSP.

The forgoing is a general commentary and is not intended to be exhaustive.

Since the beneficiary's entitlement to ODSP benefits is based on the beneficiary's ability to meet the income and asset test, a disabled family member should generally not be left an absolute gift which would have the effect that the beneficiary's assets and income exceed the prescribed limits. As noted, the most common solution for a person wishing to leave a share of his or her estate to a disabled family member is to establish a fully discretionary trust, commonly referred to as a Henson trust, based on the decision in Ontario, *Director of Income Maintenance, Ministry of Community Services v. Henson* (1987) 28 E.T. R. 121 as affirmed by the Court of Appeal (1989) 36 E.T. R 192.

According to ODSP Directive 4.7, an absolute discretionary trust is a trust whereby the trustee has "absolute and sole discretion regarding payments from the trust to the beneficiary. The trustee is not obligated to make the funds available to the person for his/her maintenance or support".

<u>SOME PRACTICE POINTS</u>

1. When drafting the trust, realize that the primary goal is to preserve the income support and related benefits that are offered under the ODSP plan for eligible persons with disabilities.

2. When administering the trust, remember that there are exempt assets and exempt income. Try to maximize the exempt assets available to support the beneficiary.

3. Create opportunities to use the exempt assets in a manner that will have the greatest possible effect on the beneficiary's standard of living. See comments below re purchase of a home, as an example.

4. Consider how exempt assets or income can be applied for the benefit of the beneficiary/benefit unit without exceeding the limits.

5. Recognize that payments towards disability-related items and services are or may be exempt and, where there is uncertainty, seek approval for expenses that may not obviously be related to the beneficiary's disability.

6. Assess the beneficiary's capacities and potential to live independently. If the evidence suggests that the beneficiary may be able to live independently with some support, then consider providing the trustee with authority to purchase a home for the ODSP recipient. The idea being that assets in the Henson trust may be used for that purpose without offending the income or asset test.

7. Where the trust owns the real estate, make the owner responsible for payment of property taxes and insurance. The argument being that payment of these expenses from the trust are not voluntary payments that go to the $6,000.00 income limit. In cases where the trust is going to own the real estate, authorize the trustee to charge the ODSP recipient rent.

   Compare this with a rental situation where every dollar contributed to rent is taken into account toward the $6,000.00 twelve month voluntary payment limit.

   Payments for utilities such as cable, internet, etc., are usage based and will generally count as voluntary payments that are subject to the $6,000.00 limit.

8. Since disability related expenses are exempt, consider whether the disabled person may need a support worker to assist him or her with daily life. In those cases, we may include a clause in the Will that allows the trustee of the Henson trust to pay wages or salaries of the support worker. The argument being that such expenses are "disability related" and, accordingly, more of the trust property can be applied for the benefit of the disabled beneficiary without offending the prescribed limits.

9. Consider that the Henson trust may come into existence when the beneficiary is under forty-three years of age. In that case, the *Accumulates Act* is relevant. Note that under the *Accumulations Act*, a trust can accumulate surplus income for up to twenty-one years after the trust is created. Accordingly, if a Henson trust is created when the disabled beneficiary is, say, thirty-five years of age, trust income can be accumulated until that beneficiary is fifty-six years of age. After that period, the trust income must be paid out.

   Care should be taken not to include the disabled person or his or her dependants as income beneficiaries since the $6,000.00 annual limit applies to all members of the benefit unit who are dependents and who reside with the disabled person. In other words, do not include the disabled person's children or issue as mandatory income beneficiaries after the accumulation period.

   Subject to nuances for special cases, we usually include a broad clause that gives the trustee the authority to distribute the surplus income among issue of the parent then living, in such manner as the trustees sees fit, and with power to exclude any issue and to make unequal distributions. The trustee would then be able to distribute the income in a manner that would not affect the disabled person's eligibility for ODSP income and benefits.

10. Finally, while this paper was focussed primarily on Henson trusts and the ODSP plan, note that there are other planning tools for persons with disabilities including expense trusts, RDSPs and "lifetime benefit trusts." The lifetime benefit trust came into effect on June 13, 2013 when Bill C-48 was proclaimed into force. This trust could be created with registered money. The basic idea is that registered funds can be used to purchase an annuity ("qualifying trust annuity") . The parent would then get a deduction for tax purposes. The funds from the qualifying trust annuity are then held in a fully discretionary trust similar to a Henson trust but only the disabled person is entitled to payments during his or her lifetime. What impact such trusts will have under the ODSP is uncertain but the significance of this type of trust is that it could lead to significant income tax savings to the parent when the parent dies.

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