Consider Special-Purpose Trusts When Facing Mental Illness or Substance Abuse

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Over the last 30 years, I have participated in more than 10,000 involuntary civil commitment hearings. Each involved someone alleged to have been so seriously mentally ill or substance-addicted that he or she could not safely remain in the community. Each involved lawyers, handcuffs and forensic examiners.

This note explains how a person with mental illness or substance addiction can create a special- purpose revocable trust to protect his or her assets from loss if the disorder causes a spell of disability.

In many ways, these trusts -which I've called "special-purpose" or "in-out" trusts – are like advance medical directives. They let a person with certain disabilities legally plan for a predictable flare-up in symptoms by establishing a trust which he or she can change or even revoke *except when the person is deemed so mentally ill that he or she cannot understand the nature of such actions.* While the person is sick, the trustee protects the assets from the individual's own excesses (often occurring in times of mania) and from victimization by third parties who see an "easy target."

The Self-Settled, In-Out Trust

When mentally capable individuals who are diagnosed with mental illness or addiction issues wish to reduce their financial risk, they can create a self-settled special purpose trust to control their own assets. The great attraction of these trusts is that the lawyer can explain that they allow the client to control his or her own financial destiny. The trust can be changed at any time except when the client is having an episode and the trustee believes the beneficiary to be irrational.

This is huge for the client because it preserves and protects autonomy. The client is the *subject who acts for himself or herself, and not the object of someone else acting "for his or her best interest."* The client (often in recovery from addiction, bipolar disorder or a recent dementia diagnosis) is in the best possible position to know what the future holds. The individual is goal-directed and anxious to make life better. When compared with the alternative, a public incapacity hearing many consider a demeaning, humiliating experience, these trusts are wonderful.

There are some finer points to consider. When the individual, or "settlor," arrives at *a* lawyer's office, a family member or friend is often brought along to serve as the proposed trustee. Because of the serious responsibility invested in such trustees, including a foreseeable duty to refuse the settlor's wishes when the settlor is ill, the lawyer should be careful to specify who the client is. It may even be in everyone's best interest to involve two attorneys so that each party can be independently advised.

While good devices, self-settled trusts are not magical charms. Only a handful of states recognize self-settled trusts as safeguarding all assets from all creditors. Even so, they provide other important security for the settlor / beneficiary. Under federal law, certain assets are immune from creditors if kept provably segregated from other assets. Personal injury proceeds, workers compensation settlements in some states (including mine), federal benefits such as SSI, and a long list of other "protected" assets can be segregated in the trust, providing a barrier to outside claims.

Because the settlor is giving so much responsibility to the trustee, it's wise to obtain a professional opinion from a licensed health or social services provider (a doctor, a licensed clinical social worker, a psychologist) to certify that the individual fully understands the trust's implications at the time of signing.

As noted above, what is different about these trusts is that the person establishing the trust knows in advance that if the trustee believes the beneficiary is experiencing an "episode," the trustee may refuse to make requested distributions. These trusts, therefore, contain "'in-out" provisions, permitting the settlor to revoke or amend the trust only when the trustee believes that the person is not incapacitated or being financially exploited.

A typical provision requires written notice to the trustee of any intention to revoke or amend. If the trustee believes the beneficiary is having a bad spell, the trustee can refuse to comply. Detailed instructions are then stated for how to resolve the problem. A "cooling off" period commences (usually 30 to 60 days). If the parties agree after that, there is no problem; the trust is amended, revoked, or continued. If the parties remain at an impasse, the trustee can be authorized to petition the court for guidance or appointment of a guardian / conservator for the beneficiary. In the meantime, the trust agreement directs the trustee to take care of the beneficiary while determining whether the trust should be dismantled, or a conservator appointed to oversee the trust's assets.

Third Party Special-Purpose Trusts

When a special-purpose trust is created with assets belonging to a parent, a sibling, or anyone other than the beneficiary or the beneficiary's spouse, it's a third party trust. *The beneficiary has nothing to do with creating this trust.* It can be either revocable or

irrevocable without having negative consequences for the beneficiary. What's important is that the beneficiary not be given any right to control the trust or the trustee, or to demand distributions. These trusts are often created as part of a family's estate planning when a child has disabilities, including serious mental illness or addiction disorders. It's not necessary that the beneficiary be "disabled" for Social Security purposes. None of the property passing into the trust will ever have been owned by the beneficiary, and except as the trustee decides to give it to the beneficiary, none will be. These are particularly helpful when any funds given to the beneficiary will be lost to creditors or substances.

Administering such trusts is a great responsibility, and it's a good idea to create a non-binding "letter of intent" to guide the trustee, who may not personally know the beneficiary. The letter of intent should outline the beneficiary's history and may include instructions about handling distributions as situations fluctuate. The settlor may wish to stipulate that certain conditions be met in order for distributions to be made. This is often stated in terms of staying on medication or remaining sober (or in rehabilitation to achieve sobriety) for a certain period.

As readers confronting these issues know, mental illness and addiction are hurricanes. Without preparation, they swallow everything in their paths. Special-purpose trusts won't stop them, but they can be a storm cellar while the winds rage. Two excellent resources for related issues related to treatment, especially the greatly recommended special psychiatric or "protest" advance medical directive, are NAMI (National Alliance on Mental Illness) and the Treatment Advocacy Center. The latter is one of my particular favorites.
