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Preparing finances now for possible cognitive decline is just plain smart

MARY GOODERHAM
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Most investors try to stay on top of their accounts and follow the rules of prudent money management. But as the mind slows with age, decision making may be impaired, and experts warn that dementia and even Alzheimer's disease can leave you incapable of managing your affairs.

"As we age, our personalities change and it's undeniable that our cognitive abilities do, too," says Marshall McAlister, a private wealth counsellor and principal at Pavilion Investment House in Edmonton.

Putting controls in place for the decline to come is becoming top of mind for many people, he says. They fear they might fall prey to fraud, for example, or begin to make mistakes with electronic banking. The wealthy are particularly at risk, as they have more to lose.

"We require older people to pass a driver's test in Canada, but that's not required for managing your finances," he says.


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KATARZYNABIALASIEWICZ/ISTOCKPHOTO

A 2016 study by Texas Tech University and the University of Michigan showed that financial literacy drops significantly as people age, matching the erosion of memory and problem-solving abilities later in life. Respondents to basic financial questions saw their test scores fall 1 percentage point each year above age 60.

At the same time, however, older people didn't report a loss of confidence in their capacity to make financial decisions, the researchers found, because the decline happened gradually and they were not aware that their abilities were degrading.

"It's not going to be optimal if you can't remember if you rebalanced [your investments] and you can't keep up with your records," says Sandi Martin, a fee-for-service financial planner at Spring Financial Planning in Gravenhurst, Ont. It makes sense for older people to designate others who can pick up the baton long before that day arrives, she says.

"We all have to prepare for the time when the optimal strategy is to let someone take over," she says. Choosing someone to take over for you can be difficult, she notes, as that person may ultimately face your feelings of paranoia, stress and worry that can come with Alzheimer's.

Everyone, especially high-net-worth individuals, must plan for incapacity, says Philip Renaud, a trust and estates lawyer and partner at Duncan Craig LLP. His clients are urged to make out wills, create enduring powers of attorney and personal directives for health care. These latter documents can vary by jurisdiction and be tailored to suit the individual or couple, for example covering specialized assets such as a family business or vacation property.

Here are steps to consider for financial planning in cognitive decline.

Form a relationship with a trusted person or people who will carry out your wishes.

Find someone in your family, or an accountant or professional adviser or lawyer who knows you and what your intentions are, who will manage your personal affairs and be your backstop, says Mr. McAlister. Many people choose their spouse for the role, he says, but a spouse can often have the same cognition decline or not be up to the job.

Mr. Renaud notes that in picking the right executor, trustee or attorney (the title given to someone who has power of attorney), beware of tension among family members. A legal representative may need specialized knowledge to deal with assets such as the family business or vacation property.

Some people hire a professional to be their executor or attorney, someone who has the right skills, is accountable and is a good record-keeper. This person could also be paired with a family member or personal friend, say, to get “the best of both worlds,” he says.

Draw up an investment policy statement and set markers for determining your competence.

This will ensure that your affairs can be picked up seamlessly and managed according to a program when the time comes.

Mr. McAlister says there are people with assets of $5-million or more who have no kind of financial plan in place and who also have outdated wills, powers of attorney and personal directives. “We have to know how all that money is going to be managed before we have to guess what your intentions are,” he says.

Setting rules up front is essential, Ms. Martin suggests. “The more that’s agreed upon ahead of time, when everybody’s thinking rationally and at their full capability, the easier it is later on.”

It’s essential to have a “test for capacity” in your power of attorney, Mr. Renaud notes. For example, the determination can be made by a doctor, a spouse or your children, although he warns that family members can have difficulty or conflicts in making such a determination.

Draw up a power of attorney that covers incapacity and ensure its rules and conditions work with your situation.

Most provinces allow for an immediate power of attorney, which applies instantly, as its name implies, and a "springing" power of attorney that can be invoked "if your memory starts to go," Mr. Renaud says. "You're still the boss and you call the shots as long as you're still capable, but this enables your attorney to step in and help you manage, and, if necessary, take over."

The wording of the power of attorney must cover special situations, he says, such as use of the family cottage or whether you want to keep donating to a charity. An attorney is typically bound by a "prudent investor rule" that might not suit a high-net-worth investor who prefers a riskier asset mix, say, or who owns a business, Mr. Renaud notes. "You can change the rules."

Consider forming a trust that will allow you, or you and your spouse, to have your affairs managed competently by a trustee.

If you're older than 65, turning all of your assets over to an alter ego trust will allow you to remain the beneficiary of all capital and income if you become incapacitated. A spousal trust works much the same way, says Mr. Renaud, noting that most people opt for trusts to avoid probate in the settlement of estates. He recommends that individuals consult with their lawyers about the advantages and disadvantages of powers of attorney and trusts in their situations.

"Think about potential problems and put in rules and systems," he says. "This will take pressure off your executor or trustee – and ensure that your wishes and family order are maintained."

Hold family meetings to disclose and discuss how your investments, banking and other affairs are being managed – and should be in the future.

"I'm a big believer that if moms and dads tell their kids what's going on, that can allow a greater experience for everybody involved," says Mr. McAlister.

Family members who are going to be responsible for managing your affairs through a power of attorney should be told your financial and investment wishes well ahead of time, Ms. Martin says, before cognitive decline brings on feelings of mistrust.

"You need to have a good, long, honest discussion so they're not just entering into it blindly," she says. "You have to say, 'Here are my wishes now, you just do the best job, and don't worry whether me in 20 years thinks you're doing a good job.'"