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Special Needs Planning for Children and Young Adults

Americans with special needs may benefit from public and private resources to support their medical care and living expenses. Individuals who meet the definition of disability can access benefits through federal and state programs. Workers who paid FICA taxes may qualify for Social Security Disability Insurance (SSDI), which is not covered in this commentary. Another program, Supplemental Security Income (SSI), is a needs-based program administered by states for those with limited resources. Generally, SSI is for children and young adults. To qualify, the disability must occur before the age of 22. Eligible individuals may receive discretionary income and Medicaid coverage for health care. The SSI program adheres to strict income and asset limits, and this is why a Special Needs Trust is valuable.

The Special Needs Trust (SNT) allows individuals with disabilities to receive income beyond the SSI amount without jeopardizing their eligibility. The trust is established by a parent, grandparent, legal guardian, or even the disabled individual – if they are legally competent to do so. The SNT document outlines the terms and conditions under which the funds in the trust can be used. Assets are contributed to the trust for the benefit of the disabled individual. Contributions may include cash, investments, real estate, or other valuable items. The grantor appoints a trustee to manage the SNT and make distributions on behalf of the disabled beneficiary. The assets and income within a properly structured SNT do not impact an individual's eligibility for programs like Medicaid or SSI.

There are two types of SNTs: third-party trusts and first-party trusts. Third-party SNTs are the most popular and are funded with assets that do not belong to the disabled individual. Established by family members, it allows multiple donors to contribute (grandparents, friends, and parents). It is a mechanism for parents and family members to gift and accumulate assets; the gifting and annual exclusion tax rules apply. It may be structured as a grantor's trust, where the grantor pays the taxes, or non-grantor trust, where the trust pays taxes on accumulated income and the beneficiary pays the taxes on distributions.

A first-party SNT is funded with the disabled individual's assets. This structure is appropriate when the disabled individual wins a personal injury settlement or receives an inheritance. The disabled individual is treated as the owner of the assets and must pay the income taxes.

SNTs come with risks. The rules are complex, and the laws vary by state. A simple mistake can disqualify the individual from government benefits. Special Needs Trust planning is a specialty for some attorneys and retaining experienced lawyers is recommended. Another risk, as with any irrevocable gift, is giving up control of assets. It is not easy to claw back funds if the SNT is overfunded. For those who are hesitant to commit to a trust structure, there are other ways of saving.

An ABLE account is a more cost effective and straightforward tool for supplementing a disabled person's government benefits. Contributions are made with after-tax dollars and are limited to 18,000 a year. Earnings grow tax-free. Distributions for qualified disability expenses are also tax-free. Total allowable contributions differ by state and range from $235,000 to $500,000. Saving in an ABLE account does not impact Medicaid benefits, regardless of how much money is in the account. However, any amount over $100,000 in an ABLE account is considered a resource of the disabled individual and may fully or partially jeopardize Supplemental Security Income (SSI) benefits

In summary, SNTs can help loved ones of disabled individuals qualify for federal and state assistance, while also supplementing their income. ABLE accounts are less complex and offer tax-deferred growth, but there are restrictions on total contributions, size, and how the distributions may be spent. If you are planning for a special needs individual, we recommend selecting a qualified attorney with in-depth knowledge of state and federal laws.

Please reach out to your Wealth Manager with questions about Special Needs Trusts.

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