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ESTATE PLANNING

Parents with disabled children benefit from special needs trusts

Families with special needs children face a variety of financial challenges. Medical care, therapy and specialized education can quickly drain family resources. One of the greatest challenges many parents face, though, is making sure their disabled children have access to appropriate care and support when they can no longer provide them.

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Fortunately, there are many government programs designed to help people with special needs, including the Social Security Administration's Supplemental Security Income (SSI) program, Medicaid and various housing assistance programs. For many disabled people, access to such assistance is crucial to their long-term well-being and survival.

But there are stringent financial requirements to qualify for most public aid, even for seriously disabled individuals. For example, to receive SSI and Medicaid assistance, disabled individuals cannot have more than $2,000 in personal assets, excluding their residence and vehicle. This makes it very difficult for disabled individuals to directly own even a relatively small amount of personal property or savings.

This problem is often compounded by well-meaning family members who gift or bequest money or other assets to a disabled child. If the amount transferred exceeds $2,000, the disabled recipient immediately becomes ineligible to receive government assistance.

The solution to this problem is a special needs trust. Also called a supplemental benefits trust, a special needs trust is a separate legal entity created to hold funds for the benefit of a disabled individual. By placing assets in a properly drafted special needs trust rather than giving them directly to a disabled child, it is possible to both provide for their continued welfare and maintain their eligibility for needed government assistance like SSI and Medicaid.

While special needs trusts often resemble standard testamentary or inter vivos trusts, they have several unique requirements. For example, for the trust to reliably safeguard the beneficiary's access to public aid, the trustee must ensure trust funds are not used to pay for basic needs such as food or shelter. Further, except under rare circumstances, the trustee cannot distribute cash directly to the beneficiary.

While the prohibition against using trust assets for basic necessities somewhat limits the usefulness of special needs trusts, there are still a variety of ways trust assets can enhance the happiness and welfare of a disabled beneficiary. For example, funds can be used to pay for otherwise uncovered medical care, rehabilitation programs, nursing and custodial care, educational programs and equipment, entertainment and travel costs.

There are three types of special needs trusts and each is subject to different, and often complex, legal requirements.

NO. 1-THIRD-PARTY TRUSTS

The most commonly used special needs trust is a third-party trust. In many respects these trusts mirror other standard trusts in that the person establishing the trust – called a grantor or settlor – grants a portion of their assets to the trust to be held and administered by a trustee for the benefit of a third party, called the beneficiary.

Although third-party special needs trusts are often established by parents for their disabled children, they can also be set up by grandparents, siblings or other relatives. In fact, they can be established by anyone interested in providing for the disabled child's current and future care.

Parents with disabled children benefit continued

Moreover, while these trusts are typically funded by outright gifts and bequests, they can also be funded by a variety of other mechanisms like life insurance.

NO. 2-SELF SETTLED TRUSTS

Sometimes a disabled person may already have assets that would prevent them from obtaining government assistance. This often occurs after a personal injury settlement or an inheritance from a well-meaning relative outside a third-party trust.

In this situation, it is still possible to establish a special needs trust to regain eligibility for government benefits, although the requirements for these "self-settled" trusts are much more stringent than for third-party trusts.

Self-settled special needs trusts are subject to a variety of legal requirements imposed under the Omnibus Budget Reconciliation Act of 1993 (42 U.S.C. 1396p(d)). For example:

- The beneficiary must be under 65 years old when the trust is established;
- The trustee must have full discretionary authority over all trust distributions;
- The trust must be drafted to expressly state it is supplemental to various public benefits and does not supplant the benefits;
- The trust must be established by a parent, grandparent, guardian or court;
- The trust must be irrevocable.

In addition, the trust must specify that when the disabled individual dies, any remaining funds in the trust must be used to pay back the government for the costs incurred in providing care to the disabled individual. Consequently, these trust rarely continue beyond a single generation since the costs of providing government care can be astronomical and almost always exceed the residual trust assets.

NO. 3-POOLED TRUSTS

The third type of special needs trust is called a pooled, or "C" trust (because it was originally authorized under 42 USC 1396p(d) (4) subsection c). Pooled trusts must be established through a nonprofit entity that administers the trust and serves as trustee. There are several such entities in Colorado, including the Good Shepherd Fund and the Colorado Fund for People with Disabilities.

The trust assets contributed by the grantor are usually kept in a separate sub-account, but pooled together with other assets held by the nonprofit for investment management and administrative purposes.

Pooled trusts may be established by anyone, including the disabled individual. And while many of the requirements outlined above for self-settled trusts apply to pooled trusts as well, there are some exceptions. For example, the beneficiary can be over age 65 when the trust is established. Further, any fund remaining in the trust after the beneficiary dies are retained by the nonprofit agency, rather than being used to repay the government for services provided.

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