

# Price & Farrington's Estate and Tax Planning FastFacts

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Estate, Tax, Retirement and Family Wealth Planning for Advisors+ Clients

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## Supplemental (Special) Needs Trusts: Frequently Asked Questions

To Our Clients, Colleagues and Friends:

**Trusts** are the most versatile tools in the estate planning attorney's toolbox. Trusts come in dozens of varieties and serve multiple estate planning purposes for people of all levels of wealth. In our monthly FastFacts articles, we have frequently addressed the breadth and scope of this topic. (All of our FastFacts articles - including those relating to trust planning - are on our website at [www.pricefarrington.com](http://www.pricefarrington.com).)

**Q. Why use a Supplemental Needs Trust? A. To preserve governmental benefits and preserve assets...** A Supplemental Needs Trust (sometimes called a Special Needs Trust — both are referred to as an SNT) is a specialized legal instrument designed to benefit an individual who has a disability. An SNT is often a "stand-alone" legal document, but it can form part of a will or revocable living trust. SNTs have been used for many years and were given an official legal status by the U.S.

Congress in 1993. (Omnibus Budget and Reconciliation Act — OBRA '93.)

An SNT allows a person under a physical or mental disability, or with a chronic or acquired illness, to have, held in trust for his or her benefit, an unlimited amount of assets. In a properly drafted SNT, those assets are not considered *countable assets* for purposes of qualifying for certain government benefits. These may include Supplemental Security Income (SSI), Medicaid, vocational rehabilitation, subsidized housing, and other benefits based upon need. An SNT provides for supplemental and extra care over and above that which the government provides.

Each SNT is its own entity with its own federal I.D. number issued by the I.R.S. According to Congress an SNT must be irrevocable. A properly drafted trust should include provisions for termination under certain circumstances and should include directions for amendment when necessary.

**Q. My family has money and we're not too concerned about governmental benefits. Why bother creating a Supplemental Needs Trust? A. To protect your disabled family member...**

Other types of spendthrift or family trusts aren't appropriate for Special Needs persons because they don't address the specific needs of the disabled beneficiary or his or her future lifestyle. Even where a family may have significant resources to help a family member, an SNT should be set up to address these issues. Assets placed in the trust remain noncountable assets and allow the beneficiary to qualify for available benefits and programs. Why give up services that might be available to your relative now and in the future? Just as important, *the trust funds aren't subject to creditors or seizure*. If the disabled



beneficiary should ever be sued in a personal injury or other type of lawsuit, monies placed in the trust are not subject to a judgment.

**Q. If having money causes problems for my disabled daughter, why can't I just leave that money to her brother so he can look after her?**

**A. Leaving money to others can create serious problems.** "Disinheriting" a beneficiary was commonly done before the use of SNTs was officially recognized by Congress. But *disinheritance* as a means of providing for a disabled or ill person puts the assets at risk. A non-disabled sibling holding assets for the benefit of a disabled sibling could be subject to liabilities such as judgments from auto accidents, a bankruptcy or a divorce, causing all of the assets to be lost. Using an SNT guarantees that the funds will be held only for the benefit of the person under the disability or chronic illness, and not for any other purpose.

**Q. What must a Supplemental Needs Trust say? A. SNTs need special language...** At a minimum, the trust should state that it is intended to provide "supplemental and extra care" over and above what the government

### Ponderables

"Every man is guilty of all the good he didn't do."

— Voltaire

"If they can get you asking the wrong questions, they don't have to worry about the answers."

— Thomas Pynchon

"Honesty is the first chapter in the book of wisdom."

— Thomas Jefferson

"Anger is seldom without a Reason, but seldom with a good One."

— Benjamin Franklin

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provides. The trust must state that it is *not* intended to be a basic support trust. It should not contain a provision called a “Crummey power”. The trust must contain the required language regarding *payback* to Medicaid.

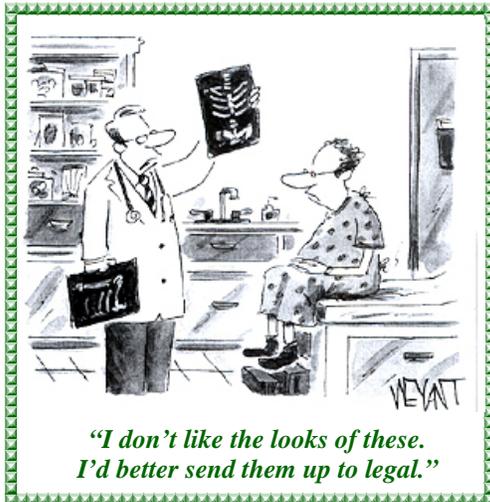
**Q. When should I create a Supplemental Needs Trust?** A SNT can be established at any time before the beneficiary’s 65th birthday. It is common to create a SNT early in a child’s life as a long term means for holding assets to benefit the disabled family member, particularly where parents want to leave funds for a child’s benefit after the parents’ deaths. The disabled or chronically ill person could at some time during his or her lifetime come into funds from third party sources, such as a personal injury settlement or a bequest from relatives or friends, Social Security back payments or insurance proceeds.

**Q. What kind of assets can be used to fund a Supplemental Needs Trust?** A. *Virtually any kind of asset*, including insurance proceeds, lump sum payments from Social Security Disability or Supplemental Security Income, settlements in legal matters or just “piggy bank” money. Money going *directly* to a beneficiary is deemed to be “*available*” and can

disqualify him or her from government benefits. In order to maintain benefits qualification, a trust is a necessity as a “safe harbor” for any assets belonging to the disabled beneficiary.

**Q. Is there an obligation to repay Medicaid or other state and federal funding sources?** A. *There may be repayment obligations in some situations.* A properly drafted trust will address the issue concerning *paybacks* to Medicaid or other such sources. The U.S. Congress mandates that repayment language must be included in all SNTs, whether repayment is required or not. The amendments to OBRA ‘93 require that a payback be made to Medicaid, but only under certain specific circumstances. *An SNT that is funded by parents or other third party sources will not be required to pay back Medicaid.* Nor will a trust funded by a personal injury settlement that is properly court-ordered into the trust. *The only assets in the trust that are subject to repayment are those assets which originally belonged to the disabled individual him or herself that are transferred into the trust.* Examples are earnings from a job, savings, certain Social Security back payments and personal injury recoveries that are not court-ordered to go into the trust. In such cases, the disabled individual’s estate might be liable for the Medicaid costs during the lifetime of the disabled or chronically ill person.

**Q. Can any lawyer create a Supplemental Needs Trust?** A. *Just as most podiatrists aren’t neurosurgeons...* It is always advisable to use an attorney with special knowledge and competence. An SNT can be very easily “invaded” by government benefit sources, and the trust can be invalidated if proper language isn’t drafted in the trust instrument. The result is a loss of benefits or savings or other financial and legal hardships for the beneficiary or trustee, some quite severe, including civil litigation or criminal prosecution in certain extraordinary circumstances. The SNT has to be properly created and, ultimately, properly defended in the event it is challenged by a court, the



Social Security Administration or Medicaid.

**Q. I have twins with Down Syndrome. Can I use one trust for both of them?** A. *Just as your children are exceptional, so are their trusts...* Each disabled individual must have his or her own trust instrument. The law requires that each SNT contain specific examples of what constitutes separate care for the beneficiary. Even twins’ needs aren’t absolutely identical. This is especially so as people get older and their abilities change.

Remember: regulations make a distinction between “First Party” (self-funded) SNTs that contain the beneficiary’s own money and “Third Party” funded trusts that contain money from other sources. First Party money is usually subject to repayment requirements. A well-drafted SNT should be able to hold money from both “First Party” and “Third Party” sources, managed in separate accounts. ■

*We wish you good planning!  
Let us know how we can help. GDP*



**Funding a Special Needs Trust With Life Insurance**

Funding an SNT with enough money to pay for the needs of a beneficiary can be a daunting task for many families. The costs of providing when the parents are no longer around exceed the resources of many families. A solution is to fund the SNT with a form of life insurance. A parent can take out a policy on his or her life to ensure that once the parent is gone, monies will be available to pay for the special needs child. The benefits? Life insurance can be paid to an SNT free of taxation. Proceeds are typically paid in a short time period, ensuring that cash is available to the child to pay for long-term care. Further, a paid-up policy will guarantee the SNT future funding while keeping the parents’ estate intact for other family members. **GDP**