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Overview of Special Needs Trusts

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A special needs trust (SNT) is a type of irrevocable trust established to hold and manage assets for the benefit of an individual with a disability or chronic illness. The primary purpose of an SNT is to provide financial support without affecting the beneficiary's eligibility for means-tested government programs such as SSI or Medicaid.

In legal terms, a trust involves the separation of legal and equitable title to property. The trustee holds legal title and is responsible for managing the trust assets, while the beneficiary holds the equitable or beneficial interest. Unlike a corporation, a trust is not a legal entity but rather a legal structure used to manage and protect assets on behalf of another.

Individuals with disabilities may qualify for government benefits and services designed to support their long-term needs, such as Supplemental Security Income (SSI) or Medicaid. However, eligibility for these programs is often means-tested, meaning that ownership of assets beyond certain thresholds either in amount or type can result in disqualification.

To preserve access to these essential benefits, assets must be held in a way that does not count as a resource under program guidelines. A special needs trust offers an effective solution. When properly drafted, an SNT allows assets to be held for the benefit of a person with special needs without jeopardizing their eligibility for government assistance.

Certain government benefits are designed to support the individual with special needs. For such programs, the SNT is designed to supplement, not supplant, the support being provided to the beneficiary. The trust is designed to provide supplemental support covering expenses not met by public programs, such as education, therapy, transportation, recreation, and certain healthcare services without replacing or interfering with the basic support provided by those programs (e.g., food, housing, or standard medical care).

As a result, provisions are drafted into the trust to pay for items and services that do not support the beneficiary but, rather, pay for items and services that are not provided by the program. The types of government programs that provide benefits for which SNTs are commonly drafted to accommodate are Social Security Disability Insurance (SSDI), Supplemental Security Income (SSI), Medicaid, and Supplemental Nutrition Assistance Program (SNAP).

The treatment of an SNT depends upon the way it was created and funded. A SNT that is created by the individual with special needs or partially funded with their assets are referred to as a first party SNT. Upon the death of the person with special needs, the assets of the first party SNT may be subject to reimbursement claims by the government to recover the funds disbursed to him or her while living. Additionally, these types of trusts may not be created after the individual with special needs reaches age 65.

When another individual or a third party creates and funds a SNT for the benefit of a person with special needs, these trusts are referred to as third party SNTs. Upon the death of the individual with special needs, the assets held in a third party SNT are not subject to any reimbursement claims by the government since the assets are not part of the decedent's estate–either at death or during his or her life. In funding a third party SNT, the grantors typically use part of their lifetime federal gift tax exclusion to fund the trust because gifts that attempt to use the annual federal gift tax exclusion amount, if done properly, would disqualify or reduce benefits and defeat the trust's purpose with a deemed distribution of funds to the beneficiary. These trusts may also be funded with life insurance proceeds by designating the trust as a beneficiary or by naming the trust as a devisee of a last will and testament.

In creating an SNT, key persons are needed to help accomplish the task of caring for the individual with special needs. The primary key person is the trustee of the trust. A trustee holds the legal title to the trust's property and is tasked with the responsibility to administer the trust's property, according to the trust's terms, for the utmost benefit of the trust's beneficiary. The person or entity selected to perform this critical role for the SNT's success should be honest, caring, and wise. For the SNT to work properly, the trustee must be given discretion in making distributions for the beneficiary; therefore, a keen knowledge of what is and what is not permissible is crucial to avoid placing the beneficiary's benefits or eligibility in jeopardy.

Another key person for the trust may be the trust protector. Although not required, the trust may provide a provision for a trust protector, which adds an additional layer of protection for the SNT against unforeseen changes in the law, political

environment, or circumstances that occur after the irrevocable trust's adoption. A trust protector may be given powers to remove or replace the trustee, change the trust's situs, determine disputes that arise, terminate the trust, or amend or modify trust provisions, just to name a few. The trust protector ideally should not be a relative, subordinate, or beneficiary, but rather a trusted advisor familiar with the beneficiary with special needs and with sharp business acumen to act as a resource and guide at critical times that come in administering a trust that will continue to exist for many years in the future.

Further, the language contained in the SNT is particularly important for the document to effectively function. Language drafted principally to address the programs the individual with special needs is seeking to receive is often best. Although federal benefits enjoy relative uniformity in their implementation across the United States, each state has its own nuances regarding their own public benefit qualification, eligibility requirements, and reimbursement claims procedures. Language in the trust that grants mandatory distributions to the beneficiary with special needs may reduce his or her benefits or may outright disqualify him or her from the program. A right of withdrawal or "Crummey power" used to create a present interest gift may have the same effect. Additionally, defining or outlining payments that may be made that do not correspond with the authorized and permissible expenditures for the benefit program may also create problems for the person with special needs.

The trust's language should be drafted to provide supplemental benefits, not support. If the trustee is directed to make dispersals for a typical distribution standard, such as for the health, education, maintenance, or support of the person with special needs, the trust will likely be deemed to be providing support rather than supplementing benefits, thereby reducing or eliminating available public assistance.

Establishing a special needs trust is a critical step in protecting the long-term well-being of a beneficiary with a disability. However, equally important is ensuring that the trust is adequately funded to allow the trustee to meaningfully supplement the beneficiary's care and quality of life. An SNT may be funded with a variety of assets, including real estate, retirement accounts, cash, investment portfolios, and other personal property. One particularly effective funding vehicle is life insurance, which can provide a dependable source of capital to support the beneficiary after the death of parents or primary caregivers.

When properly structured and funded, an SNT can coexist with government benefit programs and serve as a powerful tool for maintaining eligibility while enhancing the beneficiary's overall support. To ensure compliance with applicable laws and maximize the effectiveness of the plan, it is essential to consult with an attorney experienced in special needs planning within the jurisdiction where the individual resides.

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