



# **Supplemental Needs Trusts: The Centerpiece of Estate Planning for Parents of Children with Disabilities**

Neal A. Winston, Esq.  
Michael R. Couture, Esq.  
Andrea B. O'Brien, Esq.

440 Broadway  
Somerville, MA 02145  
Tel. (617) 841-4000  
Fax. (617) 629-7500

[winstonlg.com](http://winstonlg.com)  
[info@winstonlg.com](mailto:info@winstonlg.com)

Copyright 2013, Winston Law Group, LLC, all rights reserved.

## **I. Introduction**

The single most pressing question for parents of children with disabilities is “what will happen to our child after we’re gone?” Families are often anxious when considering the care their children will receive after the parents’ death. Understandably, many parents fear that, after their death, their child’s quality of life will suffer due to insufficient resources, the lack of effective advocacy, and the absence of the family home. Most parents, however, do not have the resources to provide quality lifetime care for their child without the assistance of government programs such as SSI and Medicaid.

While government benefit programs offer substantial services in terms of health care coverage, the available cash benefits are small. The goal, therefore, is to preserve the child’s eligibility for government benefits with additional funds available to supplement these benefits. The Supplemental Needs Trust (also referred to as the Special Needs Trust) accomplishes this goal.

## **II. Creation of the Trust**

A trust permits a person (the Settlor or Grantor) to designate a sum of money or property to be used for the benefit of another (the beneficiary). This is accomplished through a written instrument (the trust document), which transfers “beneficial” ownership of the trust property to the beneficiary. The money or property held in the trust is managed by a trustee according to the grantor’s instructions.

A Supplemental Needs Trust (SNT) is a special type of trust usually created during the lifetime of the parents of a child with a disability. The trust is established by the child’s parents (the Settlers or Grantors) and managed by the parents or another party such as a professional (the Trustee). The trust is can be revocable or irrevocable (cannot be changed or terminated), which allows a range of options related to control and taxation. If the trust is irrevocable, it will be assigned a federal tax identification number required to file an income tax return each year.

## **III. Key Terms Used in Trusts**

SETTLOR/GRANTOR:	person who creates and funds a trust
TRUSTEE:	person who manages the trust
BENEFICIARY:	person who benefits from the trust (the child)
PRINCIPAL (CORPUS):	the money or property that is held in the trust money generated by investing the principal

REVOCABLE TRUST: person who creates the trust reserves the right to amend or terminate the trust and recoup the assets

IRREVOCABLE TRUST: person who creates the trust cannot terminate or amend the trust

LIVING TRUST (INTER VIVOS TRUST): trust funded and used while the settlor is alive

#### **IV. Generally Comparing Revocable and Irrevocable Trusts**

##### REVOCABLE TRUSTS

Grantor can amend or recoup assets

Grantor pays tax for undistributed income trust earns at grantor rate

Does become a separate tax paying entity apart from the grantor

At grantor's death trust funds are part of the grantor's taxable estate

Avoids Probate

##### IRREVOCABLE TRUSTS

Grantor cannot amend or recoup assets

Taxes for undistributed income usually paid at trust tax rate

Can become a separate tax paying entity apart from the grantor

At grantor's death trust funds may not be part of grantor's taxable

Avoids Probate

The key element in a SNT is the trustee's absolute discretion in determining the timing and amount of distributions from the trust. Keep in mind that the purpose of the trust is to add to, not to replace, existing government benefits. Supplemental Security Income (SSI) and Medicaid (called MassHealth in Massachusetts) are two programs that benefit individuals with disabilities. Both SSI and Medicaid, however, have strict eligibility requirements with respect to an applicant's assets and income. Accordingly, the trustee's distributions to the child with a disability may disqualify the child for benefits.

**EXAMPLE**

Peter and Jen set up a trust for the benefit of their son, Jack. Jack receives SSI and Medicaid benefits. The terms of the trust require the trustees to pay all income from the trust to Jack on a monthly basis. Jack receives his first monthly income check from the trust in the amount of \$650. The SSI and Medicaid programs terminate Jack's benefits because he has too much income.

The trustee's power to distribute assets to the child, therefore, must be clearly limited to supplementing (adding to), but not supplanting (taking the place of), benefit programs. The trustee must be instructed to make distributions only for those items not paid for by government entitlement programs. Moreover, a limited amount of distributions from the trust paid directly to care providers for items deemed necessities (food or shelter) are considered to be the beneficiary's income for SSI purposes. For this reason, cash benefits received by the child should first be used to pay for food and shelter with trust money used to supplement these "necessary" expenses of daily living.

In Massachusetts, individuals eligible for SSI are automatically eligible for Medicaid. SSI is a federal program that provides monthly cash benefits to the elderly (age 65 or over), blind, and disabled who have \$2,000.00 or less in assets and little or no income.

**EXAMPLE**

Sally has a disability and is the beneficiary of a trust set up by her parents. Sally lives in an apartment and the trustee pays \$500 per month to the landlord on behalf of Sally. The SSI and Medicaid programs view the \$500 as 'in-kind' income to Sally. Accordingly, her monthly SSI check and Medicaid benefits may be reduced somewhat.

Distributions from the trust paid directly to providers for all other "non-necessities" (telephone bills, education, entertainment, vacations, etc.) are not considered income.

### **EXAMPLE**

In the previous example, Sally still lives in a community residence. The trustee arranges for Sally to visit her brother in Chicago by purchasing a plane ticket with money from the trust. The \$300 spent on Sally's behalf for the plane ticket is not considered income for SSI and Medicaid purposes.

### **VI. Funding of the Trust**

In a properly drafted SNT the funds in the trust are not counted as the child's assets because the child has no access to or control over the funds. Parents, or any other person, can continue to add funds into a SNT after its creation without fear of disqualifying the child from benefit programs. Relatives or friends who want to make a gift under their Will to a child with a disability should be advised to name the SNT in their Will rather than the child.

The SNT need not be created with funds sufficient to provide for the child's entire lifetime. In fact, many parents use the supplemental trust as a "pour over" vehicle that receives a portion or all of their estate upon the parents' death. Pour-over trusts are accomplished by intentionally omitting a child with a disability from receiving a direct distribution from a Will, not out of lack of love, but from a recognition of the importance of continuing the child's eligibility for government benefits. The Will then directs the transfer of funds to the previously established SNT.

### **EXAMPLE**

Dan creates a SNT for the benefit of his son Edgar who has a disability. Dan puts \$500 into the SNT when it is created. While Dan is alive, he uses his own money to make frequent purchases to enhance Edgar's quality of life. Dan provides in his Will that he has intentionally omitted his son Edgar from directly receiving any of his estate. The Will, however, directs that 25% of Dan's estate be transferred into the SNT for Edgar's benefit and that 75% of the estate be divided among Dan's three other children. In this manner, Edgar does not receive any funds directly that disqualify him from government benefits, but the SNT funds can be used on his behalf.

## **VII. Choosing a Trustee**

While every trust requires a trustee capable of managing the trust assets, the trustee of a SNT has additional responsibilities. The trustee must be willing and able to monitor the care the child receives and to devote the time necessary for understanding the child's needs and interests. A trustee that knows the child's needs and interests can prudently spend trust income in a manner that most benefits the child. Possibly of greater importance is a trustee that understands and keeps current with SSI and Medicaid regulations (or an attorney experienced in public benefits) to avoid a reduction or interruption in benefits.

For these reasons, the parents who establish the SNT will also may serve as the original trustees to ensure that the special needs of their children are addressed. Upon the parents' death, previously named successor trustees, such as relatives or friends, continue with the administration of the trust, sometimes in combination with a professional trustee specially trained in handling trusts for a disabled person.

### **EXAMPLE**

Dan and Alice set up a SNT for the benefit of their daughter Karen. In the SNT Dan and Alice name their son, Rick, as successor family trustee, and Carl, a professional trustee, as successors. Dan and Alice serve as trustees until Dan dies. Then, Alice serves as the sole trustee. When Alice becomes too ill to continue as trustee, Rick and Carl become the successor co-trustees and manage the trust.

Parents may nominate more than one individual to serve as trustee. These trustees often serve in different capacities, one as an investment advisor (financial trustee) and one as the child's personal care advisor (personal trustee).

## **VIII. Commonly Asked Questions**

### **A. Who benefits from a supplemental trust?**

The use of a SNT will benefit the developmentally disabled, the mentally ill, individuals with head injuries, and other persons with disabilities who qualify or may qualify for SSI and Medicaid. A SNT is useful in a wide range of circumstances because the funds held in trust should not be considered 'countable assets' that disqualify a child from eligibility for government benefits.

B. What do we do if we don't know a suitable original or successor trustee?

In some instances there may not be a relative or friend available to serve as the family trustee. In these situations, parents may be able to use traditional banks and professional fiduciaries as trustees. Many professional fiduciaries, however, will not get involved in trusts when the trust assets are relatively small (less than \$1,000,000). There is also often an unwillingness of a bank or similar professional fiduciary to become involved in the personal care of the child with a disability. There is a growing group of professional trust managers and trustees who specialize in public benefits, special needs, and also serve with relatively small trusts. Trust managers support parents or other family members who wish to be the sole trustees, but do not have the necessary skills or wherewithal to handle the day to day trustee duties. Professional trustees will not only manage the trust assets but have specialized knowledge to maintain public benefit eligibility, and they often have case managers available to monitor the child's medical and other personal care issues.

C. What are the alternatives to a SNT?

There are essentially three alternatives to the SNT. First, parents can intentionally disinherit a child with a disability. While disinheriting preserves eligibility for government benefits, the lack of funds designated or preserved to enhance the child's quality of life usually makes this an unsatisfactory alternative. Moreover, many parents feel uneasy and dissatisfied in choosing to disinherit their child.

The second alternative is an outright gift to the child with a disability. Once received, funds given to the child become the child's resources for SSI and Medicaid purposes. As a result the child is rendered ineligible for government benefits until the funds are exhausted. For this reason, parents should avoid this alternative.

The final alternative to creating a SNT is to leave funds to a third party, such as a brother or sister of the child, with instructions as how the funds should be used. While this alternative is relatively simple and inexpensive, the third party is under no legal obligation to use the funds for the care of the child with a disability. Moreover, unforeseen circumstances such as the divorce, financial failure, incapacity, or death of the third party may diminish or deplete the funds and thwart the parent's intentions. Thus, the uncertainties inherent in this alternative often make the SNT a more attractive option.

### EXAMPLE

Jane wants to make sure that her son Tom, who has a disability, is taken care of after her death. Jane executes a Will that intentionally omits Tom, but leaves \$80,000 to her other son Bill to be used on Tom's behalf. Jane dies and the \$80,000 is left to Bill. One year later Bill dies unexpectedly. The \$80,000 passes to Bill's wife and children (his heirs) and Tom is left with no funds to be used on his behalf.

D. How should we fund the SNT?

As stated above, the SNT need not be created with funds sufficient to provide for the child's entire lifetime. Parents will want to ensure, however, that at some point there are sufficient funds for their child's lifetime. The assistance of a financial planner is often helpful in this area. Life insurance is a good alternative funding source.

Even without a financial planner there are several steps parents can take to work toward adequate funding. Some basic options include: (1) using the SNT as a pour-over vehicle to receive a portion of the parents' estate on their death; (2) educating relatives about the SNT and encouraging gifts to the trust rather than outright gifts to the child with a disability; (3) directing income from investments to the trust; and (4) placing property, such as a family house, into the trust, with management responsibilities left to a family member or professional.

E. Can a child with a disability establish a SNT for his or her own benefit?

Under the SSI rules, a person with a disability may use his or her own funds to establish a special type of SNT, and the funds in the trust are not considered as available assets for eligibility purposes. This special type of trust must be established by the individual's parent, grandparent, legal guardian, or a court. In addition, the trust must provide that, upon the beneficiary's death, Medicaid be reimbursed for the funds it has expended for the beneficiary's care.

If only community level Medicaid is required, a person of any age can fund a trust for his or her own benefit without the special trust requirements required for SSI eligibility. Nevertheless, these self-settled trusts, usually funded by inheritances or damage awards in personal injury suits, can preserve eligibility for Medicaid and SSI.

### EXAMPLE

Randy has a disability and receives SSI. Randy's grandmother dies and leaves him \$50,000. Randy is ineligible for SSI as soon as he receives the \$50,000. The next month, Randy's parents sets up a special SNT for his benefit and Randy transfers the entire \$50,000 into the trust. Randy's eligibility for SSI should be reinstated once the funds are held by the trust.

Thus, the creation of a SNT by a child with a disability should be undertaken with great care. The usual alternative to transferring the child's assets into such a trust, however, is not very satisfying: spending-down the child's assets to the \$2,000 asset limitation used by the SSI program. In sum, SNTs created with a child's funds are a worthwhile option.

F. How can we be sure the trust funds will not be seen as our child's assets?

As stated above, a SNT must be carefully drafted to ensure that a child with a disability has no right to distributions of income or principal. The trustee must have absolute discretion over the distribution of funds. In this manner, the trust funds should not be viewed as the child's assets.

The Social Security Administration (the federal agency which oversees the SSI program) has local offices, which can at times be unpredictable. For this reason, a properly drafted SNT will contain an 'amendment clause' which calls for the reformation of the trust should the trust funds be viewed as an asset of the child due to benefit program rules changes.

G. If a parent sets up a SNT for their child will it affect the parent's eligibility for Medicaid?

Many elderly individuals rely on Medicaid to pay for the costs of nursing home care. Medicaid, however, is only available to those individuals with little or no assets. One of the major eligibility rules for Medicaid penalizes individuals who try to give away their assets in the hope of becoming eligible for Medicaid.

The Medicaid eligibility rules, however, contain an exception to this transfer rule for parents who establish trusts for a child with a disability. A special trust similar to what was described for SSI eligibility above can be created to hold the parent's assets for the benefit of their disabled child. Thus, parents can transfer as much money as they want to a SNT without fear of disqualifying themselves for Medicaid.

H. How does a family set up and manage a special needs trust?

Due to ever changing public benefit eligibility rules that often differ from state to state, only a highly qualified attorney should draft a special needs trust, especially if public benefit eligibility is or will be involved. Administration requires a combined knowledge of trust law, tax law, and public benefit law, so if the family members wish to be trustee, expert assistance should be obtained.