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Much to consider when estate plans involve individuals with special needs

We all want to make certain that, upon death, we provide assets for family members, friends and oftentimes charitable organizations.

When a beneficiary has special needs, however, additional issues must be considered. This is because, unfortunately, most services for an individual with special needs are provided through federal, state and local programs and eligibility is often based by a “means test.”

In other words, services are often only available to individuals with limited assets and limited income. Thus, a direct gift or inheritance to a special needs individual can jeopardize the individual's ability to participate in these programs and services.

Proper estate planning can help to ensure the assets transferred to an individual with special needs will not compromise the individual's ability to receive necessary benefits. A special needs trust (also known as a supplemental needs trust) is a specialized trust designed to benefit an individual who has a disability. The trust enables a person under physical or mental disability, or an individual with a chronic or acquired illness, to have assets held for the individual's benefit.

When properly drafted, the assets of a special needs trust are not considered “countable assets” for purposes of qualification for specific governmental benefits.

The trust's purpose is to provide “special” or “supplemental” care for the beneficiary over and above that which the government provides. A supplemental needs trust is an irrevocable trust and is considered its own entity with its own federal identification number issued by the IRS. Thus, the trust is not registered under the grantor's Social Security number, nor the beneficiary's Social Security number.

Whether the trust is created by a third-party or the individual

with special needs plays a critical role in determining whether the assets held in trust will be transferred to the government upon death.

Third-party supplemental needs trusts

As outlined in 760 ILCS 5/15.1, a special needs trust created by a third party (someone other than the beneficiary) for “the benefit of an individual who has a disability ... shall not be liable to pay or reimburse the state or any public agency for financial aid or services.”

However, where the trust assets are funded with the disabled individual's own property, the trust is liable. This type of third-party special needs trust can be created as a stand-alone trust instrument or as a subtrust within an individual's living trust.

For example, Jack and Diane are interested in leaving their estate for their son, Billy, who is disabled.

- Transfers at death only — If Jack and Diane are only interested in leaving assets to Billy upon their death, their respective living trusts can provide that any assets left to Billy will be allocated to a special needs trust, created within their living trusts upon the surviving spouse's death.

During Jack and Diane's lifetimes, they would have the ability to amend the trust provisions because it was created within their revocable living trusts. Upon death, their respective trusts become irrevocable and the special needs trust for Billy would be created upon the death of the surviving spouse. At that point in time, the special needs trust would obtain a separate tax identification number.

- Transfers during their lifetime and at death — Alternatively, if Jack and Diane are interested in transferring money during their lifetimes to Billy, they can create a special needs trust for Billy's benefit today. The special needs trust

THE BUZZ



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would be irrevocable and would obtain a separate tax identification number at the time of creation.

Jack and Diane's respective living trusts can also provide that any money bequeathed to Billy will be distributed to the existing special needs trust. A benefit of creating a stand-alone trust is that Billy's grandparents, aunts and uncles can easily incorporate special needs planning into their estate plans by simply distributing assets for Billy's benefit to the existing special needs trust. In addition, the special needs trust can be the beneficiary on a life insurance policy or retirement fund.

A third-party-created special needs trust would not be required to pay back the government for benefits Billy received during his lifetime. The trust (whether created as a stand-alone trust instrument or as a subtrust within Jack and Diane's living trusts) would also specify where the funds should be allocated upon Billy's subsequent death — i.e., family members, friends or charitable organizations.

The decanting amendment to Section 16.4 of the Trusts and

Trustees Act (effective Jan. 1) provides tremendous protection for beneficiaries with special needs in the situation where Billy is named the beneficiary of a trust that does not have the necessary special needs trust language. However, where funds are gifted or bequeathed to Billy outright and free of trust, the assets could compromise Billy's eligibility to participate in various programs and quickly dissipate.

Self-settled special needs trusts — OBRA trusts

Recognized in the Omnibus Budget Reconciliation Act of 1993 and governed by 42 U.S.C. 1396 p(d)(4)(A) and 760 ILCS 5/15.1, a self-settled special needs trust is created by a disabled person under the age of 65 for his or her own benefit (OBRA trusts). Similar to a third-party special needs trust, an OBRA trust is irrevocable and assets are not counted in determining a beneficiary's eligibility for public benefits. However, upon the beneficiary's death, the trust is required to reimburse the government for benefits received. The liability, however, is limited to the assets in the OBRA trust (family members and assets in a third-party special needs trust would not be reachable).

Pooled special needs trust

Governed by 42 U.S.C. 1396p(d) (4)(C), a pooled special needs trust is established and managed by a nonprofit organization for a beneficiary of any age. A separate account is maintained for each beneficiary, but the trust pools the accounts for investment purposes. Upon the beneficiary's death, the assets can be used to benefit other disabled individuals, however, any assets not retained in trust are subject to payback.

Because of the importance in preserving state benefits and the significant differences among the available special needs trusts, estate planning for individuals with special needs requires careful consideration.