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### **THIRD-PARTY SPECIAL NEEDS TRUSTS: PROTECTING AN INHERITANCE FOR A LOVED ONE WITH DISABILITIES**

Estate planning is especially vital for those who have loved ones with disabilities who receive and rely on public benefits like Supplemental Security Income (SSI) and Medicaid (called MaineCare in Maine). This includes parents and grandparents of children with special needs and spouses and relatives of older individuals residing in nursing homes and assisted living facilities. Failure to plan could come at a very high cost for the individual with disabilities who may lose critically necessary public benefits in the event that there is an inadequate estate plan or even no plan at all.

#### **An Introduction to Third-Party Special Needs Trusts**

A special needs trust (also called a supplemental needs trust) maximizes all available resources for the benefit of the individual with disabilities and may provide funds for goods and services, including: the purchase, maintenance, and insurance of a customized, accessible motor vehicle; experimental or alternative therapies not covered by MaineCare; communication equipment and computers; recreational activities, vacations, and hobbies; education and occupational training; pets and companionship; and professional services, including services from a professional trustee, accountant, or attorney.

A third-party trust is funded with the assets of someone other than the individual with disabilities, such as a parent or grandparent. This differs from a “self-settled trust” or “first-party trust,” which is funded with the assets of or legally available to the individual with disabilities.

A third-party trust may be established during the lifetime of the person who wants to provide for the benefit of the individual with disabilities. The person who establishes the trust is called the grantor or settlor. A third-party trust may also be established upon the grantor’s death in his or her estate planning documents.

The trust assets are held in the trust for a beneficiary with a disability and are administered by the trustee. The beneficiary may not serve as the trustee. The trustee could be the grantor if the trust is established during his or her lifetime. After the death of the grantor, the trustee could be a friend, family member, bank trust department or other professional fiduciary, or possibly an existing pooled trust.

A third-party special needs trust is not subject to the very strict legal requirements that govern self-settled special needs trusts. These are also called d4A trusts, payback trusts, or first-party trusts. (For more information regarding self-settled trusts, refer to this firm’s article entitled “What Professional Advisors Need to Know About Special Needs Trusts Pursuant to 42 U.S.C. § 1396p(d)(4)(A).”) In particular, there is no “payback” requirement for third-party trusts. When the beneficiary of a properly drafted third-party trust dies, if the

trust has not been exhausted, the remainder may be distributed to family, friends, or charity, according to the estate planning objectives of the grantor who established the trust.

### **Estate Planning When a Beneficiary is an Individual with Disabilities**

Planning that is not designed with the beneficiary's disability status in mind could cause the beneficiary to become ineligible for essential government benefits like SSI and MaineCare. A properly designed special needs trust promotes the comfort and happiness of the beneficiary with disabilities without sacrificing eligibility.

Some people mistakenly believe that they need to disinherit a loved one who is receiving SSI and is eligible for MaineCare and other means-tested public benefits out of fear of disqualifying the loved one for the public benefits. However, public benefits rarely provide for more than the most basic of needs. The better plan is to direct any inheritance to a third-party special needs trust.

When a third-party special needs trust is established under the terms of a will, it is a testamentary trust. The trust only comes into existence upon the death of the grantor or settlor, and the trust holds the inheritance for the benefit of the beneficiary with disabilities. A third-party trust may also be created during the grantor or settlor's lifetime and there are several benefits to doing so, including the following: a freestanding third party special needs trust can be funded during lifetime by the donor and by others, either with lifetime gifts or testamentary devises. Because the trust comes into existence at the time it is created, the grantor can see that the trust is being administered as he or she wishes. Another benefit is that the trust agreement can be amended, as appropriate, to comply with changes in the law. A testamentary trust is created through a Will after the death of the testator, and the Will is a public document; in an inter vivos trust, the trust provisions can remain private. Finally, when naming the trust as a beneficiary, it is sometimes easier to communicate with the financial institution when there is an existing trust and EIN.

### **Using Special Needs Trusts for Protection Against Long-Term Care Costs**

When one spouse is in a nursing home or otherwise facing long-term care costs, the healthy spouse should consider revising his or her will to include a testamentary special needs trust to benefit the spouse who needs care. If the healthy spouse should pass away first and no planning has been done, his or her estate will pass to the surviving spouse either by an old will devising all property to the surviving spouse or by the laws of intestacy. The receipt of those assets could disqualify the surviving spouse from public benefits. Some or all of the assets would have to be spent down before the surviving spouse would again qualify for Medicaid or SSI. To learn more about this strategy, see *Asset Preservation for Married Couples Using Last Wills and Testaments*.

Sometimes, the healthy spouse writes a will in which he or she intends to disinherit the institutionalized spouse. This is not recommended for several reasons. The most important reason is that the surviving spouse would have no right to assets that otherwise would be used to support his or her needs. Even the most trustworthy, devoted child who has promised to use an inheritance to help a surviving parent could be forced by divorce, illness, or unemployment to spend down the inheritance, leaving nothing for the special needs of his or her incapacitated parent.

### **Choosing a Trustee**

Loved ones or family members can manage the special needs trust while alive and well, if they are willing to serve and have proper training and guidance. Families or loved ones who create a special needs trust may choose a team of advisors and/or a professional trustee to serve. Whomever they choose, it is crucial that the

trustee is financially savvy, well-organized, and ethical. The trustee of a special needs trust should understand the grantor's objectives and be qualified to invest the assets in a manner most likely to meet those objectives.

## C o n c l u s i o n

Planning for a beneficiary with disabilities requires particular care and knowledge on the part of the planning team. A properly drafted and funded trust can ensure that the beneficiary with disabilities has sufficient assets to care for him or her in a manner intended by his or her loved ones, throughout the beneficiary's lifetime. Please contact us if we can assist you in planning for a loved one with disabilities.

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