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ABLE Accounts:

What Trusts and Estates Lawyers Need to Know

By Bernard A. Krooks and Benjamin A. Rubin

Individuals with special needs and their families and advisors are now able to set up ABLE (Achieving a Better Life Experience) accounts under Internal Revenue Code § 529A. These tax-free accounts do not affect an individual's eligibility for Supplemental Security Income (SSI) or Medicaid so long as certain requirements are met. Currently, at least 19 states are operating ABLE accounts and several more have announced plans to launch ABLE accounts in 2017. Most states allow out-of-state residents to open accounts. Thus, it is generally not necessary for clients to wait until their home state offers ABLE accounts to establish one. When first enacted, the ABLE law prohibited out-of-state residents from setting up accounts. In 2015, however, Congress removed this provision.

Although ABLE accounts offer many benefits, it is important to understand the applicable limitations and how they compare to special needs trusts. In some cases, it may be appropriate for an individual to have both an ABLE account and a special needs trust (SNT). Keep in mind that the individual with disabilities is generally considered the owner of the ABLE account even if a third party (parent, grandparent, among others) contributes funds to the account. There are two kinds of SNTs: first-party SNTs and third-party SNTs. First-party SNTs are funded with the assets of the individual with disabilities. By contrast, third-party SNTs are created by someone other than the beneficiary with disabilities and are a common estate planning tool used to improve the quality of life

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of an individual with disabilities while allowing that person to maintain his government benefits. A major characteristic that distinguishes a third-party SNT from a first-party SNT is that, on the death of the beneficiary, funds remaining in the first-party SNT must be used first to repay the states' Medicaid programs the beneficiary received services from for expenses incurred; whereas, in a third-party SNT there is no such requirement. Thus, at the death of the beneficiary of a third-party SNT, any remaining funds may be distributed to other family members or beneficiaries. This distinguishes third-party SNTs substantially from ABLE accounts as will be discussed further later in this article.

When considering the viability of an ABLE account for a client, it is important to remember that the onset of the beneficiary's disability must have occurred before he reaches the age of 26 (federal legislation has been introduced that would increase the age to 46). Otherwise, an ABLE account is not an option for that individual, and an SNT will be needed to protect assets in excess of government-permitted amounts. Moreover, the ABLE account is limited in terms of the amount of money that can be deposited on an annual basis; the current limit is $14,000 per year (this amount is tied to the federal annual gift tax exclusion amount), and there is a limit of one ABLE account per individual. With respect to SNTs, there is no limit on the amount of money that can be contributed and no limit to how many first- and third-party SNTs one individual can be the beneficiary of.

If the total value of an ABLE account exceeds $100,000, the individual will have his SSI eligibility suspended until the account balance returns below that level. Also, the amount of funds that may be held in an ABLE account is capped at the IRC § 529 Plan maximum in the state in which the ABLE account is open; state limits vary from approximately $250,000 to $500,000. In contrast, there is no limit to the amount of money that can be held in an SNT.

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Although there is no federal income tax deduction for funds deposited into an ABLE account, earnings on amounts held in ABLE accounts are not taxed. Several states offer state income tax deductions or credits for contributions to ABLE accounts, although some states limit the income tax benefit to residents who open accounts in their home state. Although there is no income tax deduction for contributions to SNTs, there are many tax planning opportunities available via the grantor trust provisions of the IRC and the qualified disability trust (QDT) provisions contained in IRC § 642(b)(2)(C).

Here's an example to help demonstrate the tax consequences of an ABLE account compared to an SNT. Let's assume that the ABLE account has $100,000 in it. (As a reminder this is the maximum that can be in an ABLE account without jeopardizing SSI.) Let's say there was a very healthy 10% return on the assets held in the account. The ABLE account would have $10,000 of income but have no income tax liability. Now let's consider a third-party SNT that is drafted as a QDT and therefore gets a full personal exemption of $4,050 in 2017. Also, to the extent trust money is spent for the benefit of the beneficiary, that money is considered income of the trust beneficiary. In many cases, the individual with disabilities will have very little other taxable income and therefore his own personal exemption and standard deduction will often be enough to cover the rest of the 10% return in this example. Thus, no taxes would be paid by the SNT, the individual with disabilities, or the ABLE beneficiary under this scenario. But, if money is accumulated in the SNT and not paid out to the beneficiary, then the income tax expense of the SNT could be higher.

ABLE accounts can be used only to cover "disability related expenses." These expenses include housing,

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transportation, education, assistive technology, employment, and other expenses that improve the beneficiary's quality of life and independence. It appears that these expenses will be defined quite broadly to include most expenses that the individual with disabilities may have. SNTs generally provide more flexibility, however, for the types of distributions that can be made, especially third-party SNTs that, unlike first-party SNTs, are not required to be for the "sole benefit" of the individual with disabilities.

At the death of the beneficiary of an ABLE account, there is a "payback" to the state for the cost of all Medicaid services that were provided to the ABLE account beneficiary after the establishment of the ABLE account. This is very similar to a first-party SNT except that for an ABLE account even funds contributed by third parties are subject to the payback. Further, there may be a slight distinction in the "payback" because, in some states, first-party SNTs have a payback for all Medicaid ever paid on behalf of the beneficiary since date of birth, whereas the ABLE account has a payback only going back to the date the account was established. Thus, this presents an interesting legal question on whether a first-party SNT may contribute to a beneficiary's ABLE account. Regardless of the slight differences in the payback requirements on ABLE accounts versus first-party SNTs, if someone other than the beneficiary is considering funding an ABLE account, he must carefully consider whether there are better options that would avoid a Medicaid payback on the money contributed.

An ABLE account may be particularly useful in some circumstances. For example, an individual with disabilities who works and wants to save some of his earnings above the government-benefit-allowed amounts may set up an ABLE account and use these funds at his leisure in the future without having to worry about being disqualified for his benefits. For many, this can be a great way to be independent and have a high quality of life without having to rely on others. In fact, federal legislation has been introduced that would allow ABLE beneficiaries who work to deposit more than $14,000 annually into an ABLE account.

Furthermore, distributions from SNTs are subject to SSI's in-kind support and maintenance (ISM) rules, whereas ABLE accounts are not. This provides one of the more creative uses of ABLE accounts. Because ABLE accounts can be used to pay for housing and food expenses without incurring the ISM reduction of the SSI by up to one-third, a trustee of a third-party SNT, the parents, or some other third party, may make contributions to an ABLE account that could then be used to pay for housing and food expenses without any SSI reduction.

ABLE accounts also can be useful when proper estate planning has not been done. If an individual with disabilities is receiving government benefits and is left an inheritance in someone else's will, those funds could cause the individual to lose his benefits. If the inheritance is less than $14,000 it might make sense to set up an ABLE account instead of incurring the expense of creating a first-party SNT. This could also be the case when the source of funds is court-ordered child support or a small litigation or malpractice settlement.

Another instance when an ABLE account may be quite useful is when the parents had saved less than $14,000 for a child inside of a Uniform Transfer to Minors Act (UTMA) account and the parents wish to apply for SSI and Medicaid benefits when the child turns 18. The UTMA account assets can be moved to an ABLE account before applying for benefits. In addition, many individuals receiving benefits may want to save some of their SSI or SSDI (Social Security Disability Insurance) money for a larger future expense, and the ABLE account will potentially allow them to do so up to $14,000 a year.

In many cases, parents have set up and funded 529 college savings accounts for their children at birth only to learn several years later that the child is not likely to attend college because of his disabilities. In these cases, it would be helpful if the law permitted a rollover from the 529 account to the 529A account. Although not permitted under current law, legislation is pending that would rectify this inequity.

Estate planning for individuals with disabilities is complex, and practitioners should proceed only after carefully analyzing all options, including ABLE accounts and SNTs. Each family's individual circumstances should be taken into account before deciding on the best course of action. ■

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