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Compassionate advice for all stages of life

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ABLE Accounts[1]

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Since the enactment of federal legislation authorizing ABLE ("Achieving a Better Life Experience") accounts, our office has had numerous inquiries about them. Our special needs families are excited about them, financial advisors are excited about them, and everyone has wanted to know when they will be available.

The bad news is that ABLE Accounts do not really fulfill their promise of a simple alternative to first-party special needs trusts … a great letdown for those who envisioned these accounts and those of us in special needs and elder law practices.

The good news is that they will nonetheless be very useful in some circumstances.

And the best news is that, after a wait of a year and a half from the time the federal legislation was signed into law (which itself was some ten years after some Down parents conceived of the idea), we finally have our first actual ABLE Account: on June 1, 2016, Ohio launched its STABLE Accounts.[2]

With that, let's dig in. But first, a little background: why ABLE Accounts in the first place?

What are ABLE Accounts, and Why Were They Invented?

A number of public benefits programs, notably SSI (Social Security "Supplemental Security Income") and some forms of Medicaid,[3] have asset limits. If you have countable assets (like cash) that exceed those limits by even a dollar, you are ineligible for that program. (We are talking assets here, not income.) And for many of those programs, you are disqualified if you try to get your assets down to the limit by giving them away.

So, what if a disabled person needs benefits from these programs, but is over-asset? And doesn't have enough useful things to spend down those assets on at the moment? A disabled person could be over-asset for a number of reasons: accumulated benefits, accumulated income from working,

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[2] Press release here: http://www.tos.ohio.gov/News/7601. Ohio ABLE Account website here: http://www.stableaccount.com/.

[3] Each state has its own Medicaid program jointly funded by that state and the federal government and (in theory) conforming to federal law. In Massachusetts, the Medicaid program is called "MassHealth".

gifts and inheritances, windfalls like a small lottery payoff, or settlement of an automobile accident or medical malpractice claim.

Congress's solution in 1993 was the "(d)(4)(A)" trust, sometimes called a "Medicaid payback trust," or (rarely) an "OBRA '93" trust. With this, a disabled person could put their money in the (d)(4)(A) trust, and it would not be countable. The trustee has discretion as to how to use the funds for the disabled person's benefit. The quid pro quo is that at the death of the disabled person, the Medicaid program has to be paid back for whatever it has spent on the disabled person, before anyone can inherit from it. Most people consider that a reasonable tradeoff.

But (d)(4)(A) trusts have a lot of problems, particularly for individuals who are disabled but legally competent and have the judgment and skills to manage their own funds. The disabled person can't sign the document creating the trust … only the disabled person's parent, grandparent, or guardian can do so, or it can be ordered by a court (expensive).[4] The initial funding of the trust must follow a precise sequence … the creator must seed the trust with at least a nominal amount of funds before the disabled person's funds can go into the trust. The disabled person cannot be the trustee. The disabled person cannot fund the trust once he or she turns 65. And, of course, you need a lawyer who specializes in special needs to draft it.

So the idea of those who first envisioned ABLE Accounts was: Why is this so complicated? Why do we need a trust? Why not just a bank or investment account that has a Medicaid payback that is somehow enforceable? And a good idea it was. For enforcement of the payback, someone hit on the idea to mimic 529 Plans, so that the state would be supervising the plans. And if the disabled person was not competent or appropriate to manage the ABLE Account, his or her parent, guardian, or agent under a Durable Power of Attorney could.

No lawyers. No trusts. No trustees. Control by the disabled person whose money it is, if appropriate. Great idea! What could go wrong?

Congress.

How Well Do ABLE Accounts Fulfill Their Promise? The Good, the Bad, and the Ugly.

While ABLE Accounts have some good features, they fall far short of the initial promise of freeing the disabled person from lawyers, trusts, and trustees when it comes to the disabled person's own money. What went wrong? Congress had to shape the ABLE Act so that the Congressional Budget Office would not deem it to "cost" the government too much to implement.

<u>The Good:</u>

- The ABLE Account funds, contributions to the ABLE Account, and distributions from the ABLE Account, are disregarded for public benefits purposes, with some exceptions.
- The disabled person himself or herself can open the account, unlike a (d)(4)(A) Trust.[5]

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[4] Federal legislation (the Special Needs Trust Fairness Act) is pending to allow the disabled person to create their own (d)(4)(A) trust.

[5] See fn. 4.

- The disabled person himself or herself can be the account manager and decide on what distributions are made for what purposes. Unlike a (d)(4)(A) Trust, no third party is needed in this role.
- All growth in an ABLE Account is income-tax free.
- Distributions for Qualified Disability Expenses (QDE) are income-tax free.
- Distributions for QDE are not countable income for public benefits programs under federal law, except for distributions for housing expenses.[6]
- *Not so good as we thought?* This "distributions not countable for public benefits programs" feature also appeared until recently to be important for someone whose primary public benefit is Section 8 housing, because many housing authorities have regarded pretty much any distribution, cash or in-kind, to be income for Section 8 purposes, thus increasing rent by 30 percent of the amount distributed. However, the *DeCambre* case [First Circuit, June 2016] has just ruled that it is only actual income distributed from a (d)(4)(A) trust that should be countable; thus, the importance of ABLE accounts for Section 8 beneficiaries may be a good deal less than initially thought.
- Contributions by third parties like Mom, Dad, or Grandma qualify for the annual gift tax exclusion (presently $14,000 per donee per year, adjusted for inflation). This is not true for gifts to (d)(4)(A) trusts, nor for gifts to third party Special Needs Trusts.
- The Designated Beneficiary of the ABLE Account can be changed to a different disabled family member.
- There is no age 65 limit on the disabled person funding his or her ABLE Account.

<u>The Bad:</u>

- ONLY the disabled person can open the account, or the disabled person's Agent under a Durable Power of Attorney, legal guardian, or parent.
- Since the disabled person is usually in a low or zero income tax bracket, the income tax benefits may be little or none.
- In order to open/fund an ABLE Account, the disabled person must presently be on SSDI or SSI, or file a Disability Certification with the Social Security Administration. A (d)(4)(A) trust can be funded without such documentation.

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[6] This feature could be very important, for example, for someone whose primary public benefit is Section 8 Housing. Many Housing Authorities consider almost any distributions from trust to be countable income for Section 8 purposes, even if the trust was a (d)(4)(A) Trust funded with the disabled person's own money, thereby raising a person's rent by thirty cents for every dollar distributed from trust … effectively a 30% tax. By having an ABLE Account instead of a (d)(4)(A) Trust, the ABLE Account could be used to purchase everything but housing costs (e.g., food) without increasing the disabled person's rent.

This feature also makes administering an ABLE Account much more convenient in some respects than a (d)(4)(A) Trust. For example, it is very important to distribute little or no cash to a beneficiary of a (d)(4)(A) Trust who is on SSI. Even though the (d)(4)(A) Trust funds are the beneficiary's own money, when it is received by the beneficiary in the form of cash it is considered income to the beneficiary, reducing SSI dollar for dollar after a $20 per month threshold. But an ABLE Account could distribute cash to appropriate beneficiaries without creating an income problem. Of course, the distribution cannot be so large as to cause the beneficiary an asset-limit problem.

- A disabled person can have no more than one ABLE Account. Any additional accounts simply do not qualify. Although states and financial institutions are supposed to design and implement safeguards so this does not happen, it presents a potential pitfall.
- The disabled person (or his/her guardian, etc) cannot direct investments of the account more than two times per calendar year, and the range of investment options are determined by the State.
- Distributions other than for QDE are subject to income tax (under the annuity rules), and an additional penalty of ten percent of the amount so distributed.
- And, of course, like the (d)(4)(A) Trust, there is the Medicaid Payback on the death of the disabled account owner. However:
    - <u>Not so bad:</u> Where the funds come from the disabled beneficiary himself/herself, we really don't consider the Medicaid Payback an evil so much as just a give-and-take. "We, the government, will ignore your excess funds, and the tradeoff is, if there is anything left over at the end of day, you pay us back."
    - <u>Good:</u> And there is actually something good here. With a (d)(4)(A) Trust, the Medicaid Payback is for all medical assistance under the Medicaid program ever received, even if the (d)(4)(A) Trust was established and funded long after Medicaid benefits began. But the ABLE Account only requires payback for medical assistance paid by the Medicaid program *after* the ABLE Account was established. For some people, this could be an important difference.

<u>And the Ugly:</u>

- The owner/disabled person must be disabled prior to attaining the age of 26.[7] While this includes a large number of the clients we serve, it excludes a large number of people with adult-onset disabilities, diseases, and injuries, without any policy justification. And, it may be difficult for older persons to prove their disability onset was prior to age 26. (d)(4)(A) trusts have no such age requirement.
- Any amounts in the ABLE Account in excess of $100,000 are countable for SSI purposes (but not for Medicaid purposes). Again, there is no policy justification for this, only attempts to conform to fiscal scoring constraints. (d)(4)(A) trusts have no such limits. A bad side effect of this decoupling of the SSI rules versus Medicaid rules is that this may cause problems in the majority of states known as "SSI" or "1634" states (like Massachusetts), where a determination of SSI eligibility results in automatic Community Medicaid eligibility (but not nursing home Medicaid eligibility).
- Annual contributions from all sources combined, including the disabled person, cannot exceed an amount equal to the annual gift tax exclusion ($14,000, adjusted for inflation). This is especially difficult to understand from both a policy and a fiscal perspective. It makes ABLE Accounts unusable in a large number of cases as a repository for the disabled person's own funds. And what is the point in discouraging third party funding, when that

[7] Proposed legislation in Congress would raise the age to 46 from 26. There are other proposals in Congress to improve the usefulness of ABLE Accounts, but of course they are just proposals.

third party funding is unnecessarily subjecting itself to Medicaid payback, which is a fiscal benefit to the government? (d)(4)(A) trusts have no such limitations.

- Aggregate contributions from all sources, including the disabled person, are limited to the state's aggregate contribution limit for 529 Plans ($375,000 in Massachusetts). (d)(4)(A) trusts have no such limitations.
- A (d)(4)(A) Trust has no restrictions on what goods or services it can buy for its beneficiary (although *how* it makes those distributions may affect the disabled beneficiary's eligibility for some programs). But an ABLE Account can only be spent on "Qualified Disability Expenses," or QDE, without incurring income-tax and a 10% penalty.
    - Ugly: On the one hand, the statutory language of QDE is restrictive for a large number of disabled persons. QDE is defined as: "Any expenses related to the eligible individual's blindness or disability which are made for the benefit of an eligible individual who is the designated beneficiary, including the following expenses: education, housing, transportation, employment training and support, assistive technology and person support services, health, prevention and wellness, financial management and administrative services, legal fees, expenses for oversight and monitoring, funeral and burial expenses, and other expenses, which are approved by the Secretary under regulations and consistent with the purposes of this section."
    - Or … not Ugly? On the other hand, Proposed Regulations from the IRS interpret QDE very liberally and broadly, in ways even more broadly than a (d)(4)(A) trust, which strictly limits any incidental benefit that may accrue to anyone other than the disable person. The IRS has concluded that QDE "should be broadly construed to permit the inclusion of basic living expenses and should not be limited to expenses for items for which there is a medical necessity or which provide no benefits to others in addition to the benefit to the disabled individual."[8] The Proposed Regulations include in QDE "expenses that are for the benefit of the designated beneficiary in maintaining or improving his or her health, independence, or quality of life."[9]

[8] Preamble to §529A Proposed Regulations, Fed. Reg. Vol. 80, No. 119, p. 35602.

[9] Prop. Reg. §1.529-A(1)(b)(16). "Such expenses include, but are not limited to, expenses related to the designated beneficiary's education, housing, transportation, employment training and support, assistive technology and related services, personal support services, health, prevention and wellness, financial management and administrative services, legal fees, expenses for oversight and monitoring, and funeral and burial expenses, as well as other expenses that may be identified from time to time in future guidance published in the Internal Revenue Bulletin. See § 601.601(d)(2) of this chapter. Qualified disability expenses include basic living expenses and are not limited to items for which there is a medical necessity or which solely benefit a disabled individual." Prop. Reg. §1.529-A(2)(h)(1).

When Might ABLE Accounts be Useful?

There is a lot of chatter and writing going on about using ABLE Accounts for OPM (Other People's Money). It cannot be emphasized enough that even though ABLE Accounts are modeled in part after 529 Plans, which *are* designed to be funded with OPM, ABLE Accounts are ***not*** a substitute for third-party Special Needs Trusts used in estate planning (see "Sidebar – There Are Two Kinds of Special Needs Trusts"). There are many reasons, including the tiny contribution limits, but the Medicaid payback alone is reason enough not to leave assets to a disabled person via an ABLE Account in most circumstances. ABLE Accounts will probably have somewhat more use as a vehicle for small gifts from Other People than as a receptacle for bequests.

So, what are some circumstances where an ABLE Account might make sense? Here are a few of our thoughts, keeping in mind always that the disabled person has to meet the various qualifications, such as onset of disability prior to attaining the age of 26, and the contribution limits and SSI limits.

- Where a disabled person has come into a relatively small sum of money that cannot be spent down within the month of receipt on useful goods and services. Examples could be small lottery winnings, small inheritances, or small settlements, such that even after spending on useful things, there is money left over (but not more than $14,000!). A (d)(4)(A) Trust can be impractical for such small amounts.
- Where Other People would like to make small gifts to the disabled person without worrying about filing a gift tax return.
- Where Other People want to make a gift to or leave a bequest to the disabled person that is too small to justify creating a third-party special needs trust.
- Where the disabled person is well-able to manage his or her own funds, and places a premium on control and autonomy (for amounts within the $100,000 or $375,000 limit).
- Where a disabled person accumulates wages and income or SSI benefits over time, and would like a convenient place to sweep amounts in excess of $2,000.

Sidebar – There Are Two Kinds of Special Needs Trusts

A lot of people don't know this, but there are two distinct kinds of Special Needs Trusts. One is the (d)(4)(A) trust we've described in the article. The vast majority of the time, it is intended to hold the disabled person's own funds; in other words, it is intended to be a "first party special needs trust." Normally a person cannot fund a trust for their own benefit and yet have the trust be non-countable for public benefits purposes, but because of the Medicaid payback tradeoff, the (d)(4)(A) trust is an exception.

The other kind of Special Needs Trust is intended for OPM – "Other People's Money". In other words, it is a "third party special needs trust." This kind of trust we often call a "Supplemental Needs Trust," but really both kinds are sometimes called "special needs trusts" and both are sometimes called "supplemental needs trusts." A third party Special Needs Trust has no Medicaid payback provision, and is intended to hold assets given to the disabled person by others. It's most common use is for the parents' estate plan, to hold assets the parents leave at their deaths for their disabled child.

- When a key public benefit is Section 8 housing (although this advantage of ABLE accounts now seems much less than originally thought due to the *DeCambre* case.)
- Where a young disabled person has a small Uniform Transfers to Minors Act account (a "custodial" account), and expects to apply for SSI at the age of 18. The UTMA account would be a countable asset for the disabled person.
- Where a disabled person wants to save for a major purchase of a service or non-countable asset (e.g., a home, car, or wedding), without the cost and complexity of setting up a (d)(4)(A) Trust.
- Where a disabled person is over the age of 64, with no available pooled trust in his/her location, or with local rules against funding a pooled trust when over age 64.[10]
- Where a disabled person is a resident of a state with onerous rules regarding (d)(4)(A) trusts (e.g., New Jersey, which requires state pre-approval for all expenditures of more than $5,000).

Open Question: Distributions from (d)(4)(A) to ABLE

When there is a larger (d)(4)(A) trust or a third-party special needs trust, can those trusts directly distribute to an ABLE account for the beneficiary from time to time to give the beneficiary some control and autonomy, and to avail ourselves of other benefits of ABLE accounts, such as non-countability of distributions other than for housing expenses respecting SSI? There are no regulations or other authority on this question.

The Social Security Administration reportedly intends to issue POMS that permit distributions from a (d)(4)(A) Trust directly to an ABLE Account for that same beneficiary.

However, recall that a (d)(4)(A) Trust must be for the "sole benefit" of the disabled beneficiary during his or her lifetime. In contrast, the designated beneficiary of the ABLE account can be changed to a different disabled family member. On its face this would seem to be a distribution from the (d)(4)(A) that would (potentially) not be for the sole benefit of the disabled beneficiary.

One could argue that if the ABLE Account distributed to the beneficiary, the beneficiary would then be free to make a gift to the disabled family member. However, unless this were a child of the disabled beneficiary,[11] this would be a disqualifying transfer for SSI purposes.

However, because the ABLE Act states that transfers to an ABLE Account are to be disregarded for public benefits law, it appears to the authors that transfers from a (d)(4)(A) to an ABLE Account should be permissible without violating the (d)(4)(A) sole benefit rules and without creating a disqualifying transfer.

A further question is: if allowed, would a distribution from a (d)(4)(A) trust to the ABLE account be nonetheless (to the extent the distribution constituted income of the (d)(4)(A) trust) deemed

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[10] As we stated in the sidebar, there are two kinds of special needs trusts: first-party (a (d)(4)(A) Trust) and third-party. Actually, and at the risk of over-complicating this paper even more, there is a second flavor of first-party special needs trust, called a "pooled trust." A pooled trust is like taking a lot of a (d)(4)(A) trusts for different beneficiaries, and having them all run by one non-profit trustee. In fact, the pooled trust statute is nearby at (d)(4)(C). Some states restrict funding of pooled trusts to when the disabled beneficiary is under 65, others (like Massachusetts) do not.

[11] 42 USC §1396p(c)(2)(B)(iii)

income for Section 8 purposes? While contributions to an ABLE Account are to be disregarded, distributions from a (d)(4)(A) Trust are not necessarily disregarded.

Are ABLE Accounts Available Yet?

Ohio became the first-in-the-nation to offer ABLE Accounts on June 1, 2016. It was followed by Tennessee on June 13, 2016, Nebraska on June 30, 2016, Florida (Florida residents only) on July 1, 2016, and Michigan on November 1, 2016. Sites: stableaccount.com; abletn.gov; enablesavings.com; myablesavings.com; miable.org/. For a chart comparing the four state plans' provisions, *see*: http://tinyurl.com/ASNP-ABLEchart

So what does this mean for residents of other states for whom an ABLE account is appropriate and good? Should that person sign up for an Ohio or Tennessee account?[12]

Our answer is: if it isn't urgent, wait for some developments to occur on two fronts.

First, there are no other plans right now to compare. (For updates, see the website of the ABLE National Resource Center at www.ablenrc.org/)**.** Each plan will have somewhat different advantages and disadvantages, and it would be nice to wait so you can shop around and compare. Remember, your clients can only have one ABLE account. Make sure the plan the client signs up for permits a transfer to a different ABLE account so they can switch to a different plan in the future if they want to.[13]

The second point has to do with whether the non-countability of the account will be recognized in Massachusetts, and by the various federal agencies that administer the federal public benefits programs. Of course they *should* … the federal law says so.[14]

But we do not as of yet have all of the changes to federal regulations and other federal rules that the ABLE statute mandates. As noted, the Treasury Department has issued proposed 529A regulations,[15] and subsequent assurances as to certain aspects of the final regulations,[16] but we do

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[12] Initially, an ABLE Account had to be a creature of the owner's state of residence. However, the law was changed in late 2015, so that now there is no longer a residency requirement. (P.L. 114-113 Consolidated Appropriations Act, 2016 [PL114-113 12/18/2015], Division Q(III)(A), Section 303.)

[13] A rollover from one ABLE Account to another is permitted by withdrawing all of the funds from the first ABLE Account, closing that account, and then depositing the funds into a new ABLE Account within 60 days. IRC §§529(b)(2)(B), 529(c)(1)(C). However, this is both troublesome and risky; it is better if the ABLE Account permits direct transfer from that ABLE Account (simultaneously closing it) to new ABLE Account.

[14] Initially, an ABLE Account had to be a creature of the owner's state of residence. However, the law was changed in late 2015, so that now there is no longer a residency requirement. (P.L. 114-113 Consolidated Appropriations Act, 2016 [PL114-113 12/18/2015], Division Q(III)(A), Section 303.)

[15] June 22, 2015.

[16] IRS Notice 2015-81 (November 20, 2015). Final Regulations will:

(1) Allow the Owner to file a certification that he or she has a written diagnosis that would meet the requirements of a Disability Certification, rather than filing a Disability Certification. This relieves the financial institution of the HIPAA implications of handling medical information, as well as responsibility of making a determination of disability.

(2) Remove the requirement that the financial institution collect the Taxpayer Identification Number of contributors (other than the Owner), if the financial institution has systems in place to reject or immediately return excess contributions.

not yet have the final regulations. Fortunately, the IRS has stated that the states and financial institutions may rely on the proposed regulations, although some may be reluctant to do so.

More importantly, the various federal public benefits programs are not all yet in compliance with the ABLE statute. Social Security has amended its Program Operations Manual System (which are not regulations but might as well be),[17] and the USDA issued guidance to the states regarding SNAP (the food stamp program).[18] But I have been unable to find anything from some other important federal programs, such as Section 8 Housing (HUD) and Veterans Aid & Attendance (Department of Veterans Affairs).

Most importantly, the Massachusetts state agency administering the Medicaid program – MassHealth – has not amended its regulations to recognize the public benefits characteristics of ABLE Accounts.[19] MassHealth is required to comply with federal law; however, from a practical perspective, it is entirely possible that an applicant for a MassHealth program with an asset limit (such as a Home and Community Based Waiver Program) and having an ABLE Account based in another state could be improperly denied due to MassHealth following its own (out of date) regulations. While in our opinion the applicant in that case should be able to win on appeal and be approved, the appeal could be lengthy and expensive, and could have to go through many levels of an administrative appeal and then the courts. If your need for an ABLE Account is not urgent and you are on or need a MassHealth program that has an asset test, you don't want to be this "test case." It might be best to wait for MassHealth to amend its regulations.

Conclusion

ABLE Accounts definitely have uses for the right people under the right circumstances. However, special needs families should still always have as part of their estate planning a third party Special Needs Trust, and just in case a (d)(4)(A) trust on standby, even if it may never be needed. In any event, disabled persons and their families still need specialized legal counselling; indeed, now that we have yet another option to choose from (ABLE Accounts), that counselling is more important than ever.

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(3) Remove the requirement that the financial institution distinguish and track what expenditures were for housing expenses, qualified disability expenses, and other expenses. The Owner alone will be responsible for correct reporting.

[17] SSA POMS SI 01130.740, effective December 18, 2015.

[18] Letter dated April 10, 2016 to all SNAP Regional Directors from Lizbeth Silbermann, Director, Program Development Division, Supplemental Nutrition Assistance Program, United States Department of Agriculture, giving guidance to states that ABLE accounts are non-countable.

[19] Massachusetts enacted legislation, prior to the federal amendment permitting a resident of one state to open an ABLE Account offered by another state, enabling the Commonwealth to *offer* ABLE Accounts, but delaying that day until MassHealth (Medicaid in Massachusetts) so amends its regulations. Since that federal amendment, whether a state can or does *offer* ABLE accounts is irrelevant to the federal public benefits treatment of an out-of-state ABLE account owned by a disabled resident of that state.