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ABLE Act Accounts: Achieving a Better Life Experience for Individuals with Disabilities with Tax-Preferred Savings (and the Old Reliable Special and Supplemental Needs Trusts)

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ABLE ACT ACCOUNTS: ACHIEVING A BETTER LIFE EXPERIENCE FOR INDIVIDUALS WITH DISABILITIES WITH TAX-PREFERRED SAVINGS (AND THE OLD RELIABLE SPECIAL AND SUPPLEMENTAL NEEDS TRUSTS)

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Under Mr. Rephan's direction, Joelle analyzed complex issues involving special and supplemental needs trusts, Medicaid estate recovery, and Medicare and Social Security Disability benefits. Joelle thanks Mr. Rephan for his guidance and expertise. She also thanks Nathan Langhurst for the many miles of bicycle rides that made good ideas great.

I. INTRODUCTION

Estate and benefits planning is a complicated topic for any client. There is no shortage of instruments that can be used to distribute assets to chosen family members while still providing income streams to the individual—IRAs, trusts, wills, joint accounts, to name several. But this planning landscape becomes imminently more difficult when the client either has a disability himself or herself or his or her chosen family members and friends include individuals with disabilities. A disability within a family creates difficult immediate and future complexities: how do we provide for this individual now; how do we provide for this individual after we are retired and no longer earning money; how do we provide for this individual after we pass on?

For example, a retirement-ready client seeking help with his or her estate plan and retirement benefits may also be continuing to provide care for his or her adult child with a disability. However, strict asset and income rules for Medicaid and Supplemental

Security Income (SSI)[1] mean that outright gifts to the individual with a disability either during or after the client's death create eligibility problems for the individual with a disability. And loss of eligibility for these programs means loss of income streams that are crucial for the individual's continued health after the retirement-ready client can no longer provide care.

Simultaneously, the benefits provided by these programs are clearly defined, and in the case of SSI, arguably inadequate: fairly generous but not an unlimited set of medical benefits from Medicaid and about $733 per month for SSI.[2] As such, clients may wish to plan their estates around these asset limits not only for their own benefit if they are disabled themselves but also for or for the benefit of a child, grandchild, or even friend with a disability.[3]

Lawyers have helped to address this income gap with various legal tools, including Medicaid Qualifying Trusts (which are actually Medicaid *disqualifying* trusts),[4] individual special needs

1. An individual with a disability can have only $3,000 in assets in order to qualify for Medicaid. MINN. STAT. § 256B.056, subdiv. 3 (2014). SSI eligibility is even stricter with a limit of $2,000. 42 U.S.C. § 1382(a)(3)(B) (2012); *see also* U.S. SOC. SEC. ADMIN., 2015 SOCIAL SECURITY CHANGES 2 (2014), https://www.ssa.gov/news/press/factsheets/colafacts2015.pdf.

Note that under Medicaid (or Medical Assistance in Minnesota) countable assets exclude the following: a single automobile used for transportation; the primary residence if the spouse, dependent, sibling with equity interest, or adult-child caregiver still lives there (or up to $534,000 in equity as of 2014 for institutionalized long-term care recipients with no one occupying the home); household goods and certain personal effects; prepaid burial spaces, burial funds (capped at $1,500 each for the recipient and the recipient's spouse), prepaid funeral trusts ($2,000), life insurance or annuity-funded burial arrangements under contract; capital and operating assets for a business as necessary to earn income; Community Spouse Allowance for well spouse ($33,851 to $119,220 for 2015); and special or supplemental needs trusts. Note, however, that the home is excluded for any Medicaid applicant who still lives in the home, but it will be counted if no one is living in the home. MINN. STAT. § 256B.056, subdiv. 2.

2. Robert B. Fleming, *The ABLE Act—A New Tool for Special Needs Planning*, VOICE NEWSL., Apr. 2015, http://www.specialneedsalliance.org/the-voice/the-able-act-a-new-tool-for-special-needs-planning/.

3. *See* Robert Fleming & Stuart Morris, *Taxation of Special Needs Trusts*, NAELA Q., Summer 2001, at 18 (providing that public benefits are insubstantial and that trusts have been used to supplement this below-subsistence income).

4. *Cf.* 42 U.S.C. § 1396a(k) (1986) (repealed 1993). Because Medicaid Qualifying Trusts (MQTs) have long since been amended by the Omnibus Budget Reconciliation Act of 1993 and will generally not apply to new estate plans, they have been mostly omitted from this discussion. However, the enterprising elder

trusts,[5] pooled special needs trusts,[6] and third-party supplemental needs trusts.[7] Another tool was added on December 19, 2014, when President Obama signed into law the Achieving Better Life Experience (ABLE) Act.[8] Modeled after the IRS's 529 accounts for tax-preferred tuition savings,[9] the new ABLE accounts[10] offer the same tax-preferred savings to individuals with disabilities to save cash-only assets, while still maintaining eligibility for SSI and Medicaid.[11] These ABLE Act accounts are the newest additions to the disability planner's toolbox. Because of the various limitations on the preceding disability planning instruments, the ABLE accounts were long awaited.[12] Yet, the legislative process resulted in ABLE accounts that are now more limited than was first envisioned.[13] As a result, these accounts are only one tool among the old standbys.[14]

This article provides a very basic overview of the new ABLE accounts and the role they play in assisting elderly clients in planning for their own disabilities or for the disability of a family member. Part II provides a brief background on the requirements of traditional disability planning devices, including individual special needs trusts, pooled special needs trusts, and third-party supplemental needs trusts.[15] Part III provides an overview of the ABLE Act in terms of its general restrictions and parameters;[16] its tax provisions, including monitoring;[17] its Medicaid payback

law attorney should be aware of these old rules and how new transfers to trust exceptions to the MQT rules could implicate the old MQT rules. *See* CTRS. FOR MEDICARE & MEDICAID SERVS., STATE MEDICAID MANUAL § 3259.2 (1994).

5. *See infra* Section II.A.1.

6. *See infra* Section II.A.2.

7. *See infra* Section II.B.

8. Robert F. Brogan et al., *Able Act Passes*, EP MAG., Feb. 2015, at 42, http://www.specialneedsalliance.org/wp-content/uploads/2015/02/EP-ABLE-article.pdf.

9. *See generally* I.R.C. § 529 (2015).

10. These accounts are also known as 529A accounts as they are fully described in section 529A of the Internal Revenue Code. *Id.*

11. *Id.*

12. Brogan et al., *supra* note 8, at 42.

13. *Id.* The ABLE account was first considered in 2008 and had no contribution limits, much like its disability planning predecessors: special needs and supplemental needs trusts. *Id.*

14. *See id.* at 44.

15. *See infra* Part II.

16. *See infra* Section III.A.

17. *See infra* Section III.B.

provision and its limits;[18] and when Minnesota residents can expect to start using ABLE accounts.[19] Part IV finishes with an analysis of the new ABLE Act accounts, how the Act compares with the traditional disability planning tools such as special and supplemental needs trusts, and what spot the Act occupies in the estate planning toolbox, ultimately concluding that the structure of the new ABLE accounts is restrictive enough that ABLE accounts do not serve as replacements for the traditional disability planning tools, but that ABLE accounts' tax savings may be worth taking advantage of in certain circumstances.[20]

II. THE BEDROCK TOOLS: SNTS

A. *Special Needs Trusts (Individual and Pooled)*

The Omnibus Budget Reconciliation Act of 1993 (OBRA '93) established general rules for the treatment of revocable and irrevocable trusts in determining Medicaid eligibility.[21] OBRA '93 generally prohibits the use of self-settled trusts—trusts established by the beneficiary of the trust (or someone authorized to establish the trust in the name of that beneficiary)[22]—to shelter assets in an effort to receive public welfare benefits while also maintaining an individual's wealth.[23] However, OBRA '93 does create two exceptions to this rule: the individual special needs trust[24] and the

18. *See infra* Section III.C.

19. *See infra* Section III.D.

20. *See infra* Part IV.

21. John J. Campbell, *Basic Strategies for SSI Planning*, 1 NAELA J. 311, 315–16 (2005).

22. 42 U.S.C. § 1396p(d)(2)(A) (2012) (encompassing the following individuals in the idea of a self-settled trust: "[t]he individual [establishing the trust][,] [t]he individual's spouse[,] [a] person, including a court or administrative body, with legal authority to act in place of or on behalf of the individual or the individual's spouse[,] [a] person, including any court or administrative body, acting at the direction or upon the request of the individual or the individual's spouse.").

23. *Id.*

24. *Id.* § 1396p(d)(4)(A) (exempting from the general rule "[a] trust containing the assets of an individual under age 65 who is disabled . . . and which is established for the benefit of such individual by a parent, grandparent, legal guardian of the individual, or a court if the State will receive all amounts remaining in the trust upon the death of such individual up to an amount equal to the total Medicaid paid on behalf of the individual under a State plan under this subchapter").

pooled special needs trust.[25] These exceptions, however, are very specific and fraught with restrictions that make their use by individuals with disabilities challenging and sometimes inflexible to say the least.

1. *Individual Special Needs Trusts*

The special needs trust is useful to an individual with disabilities because trusts generally have no limit to the amount or kind of assets that can comprise the corpus. Additionally, an individual with disabilities funds the special needs trust with his or her own assets.[26] However, special needs trusts are *not* the typical flexible grantor trust: special needs trusts[27] generally are best understood as a kind of "irrevocable discretionary trust,"[28] and therefore significantly restrict the control and direction of trust assets. Beyond these general restrictions, the grantor with a disability must be under age sixty-five.[29] Further, the special needs trust can be established only by a "parent, grandparent, legal guardian of the individual, or court,"[30] which means a person with a disability cannot establish his or her own special needs trust.[31]

25. *Id.* § 1396p(d)(4)(C).

26. *Id.* § 1396p(d)(4)(A).

27. Although these special needs trusts are sometimes referred to as "supplemental needs trusts," the two should not be confused. The supplemental needs trusts referred to in this article are settled by a third party and were used prior to OBRA '93, and are still unaffected by it. *See* 1 JOAN M. KRAUSKOPF ET AL., ELDERLAW: ADVOCACY FOR THE AGING § 11:55, n.1, Westlaw (database updated Nov. 2015) (citing Susan G. Haines, *The Cheshire Cat's Grin, or the Curiouser Case of OBRA 93*, 7 NAELA Q. 31, 37 (1994)); *see also* 1 WILLIAM CAMPBELL RIES, REGULATION OF INVESTMENT MANAGEMENT & FIDUCIARY SERVICES ch. 11, subdiv. 64 (2014) (noting that third-party-funded supplemental needs trusts are also called "Common Law Discretionary Trusts" and that "this subset of Special Needs Trusts have their origin in state law . . . ."); *infra* Section II.B.

28. A. Frank Johns, *Perspectives on Elder Law: Legal Ethics Applied to Client-Lawyer Engagements in Which Lawyers Develop Special Needs Pooled Trusts*, 29 WM. MITCHELL L. REV. 47, 49–50 (2002); *see also* John J. Campbell, *supra* note 21, at 315–16 ("Nevertheless, there is an implied Congressional [sic] intent that the trusts remain 'supplemental' and discretionary."); DEP'T HEALTH & HUM. SERVS., HEALTH CARE FINANCING ADMINISTRATION'S STATE MEDICAID MANUAL, HCFA-Pub. 45-3, Transmittal No. 64 § 3259.8A (1994) (noting that the distribution standard of a special needs trust is "discretionary").

29. *Id.* § 1396p(d)(4)(A).

30. *Id.*

31. 1 KRAUSKOPF ET AL., *supra* note 27, § 11:55 ("The disabled individual is

Moreover, special needs trusts distributions must be put toward expenses that are not covered by government benefits.[32] Yet another restriction of this kind of trust is that the trustee cannot provide funds directly to the beneficiary but must instead pay the vendor directly.[33] These restrictions are hard to understand for a person with a physical disability but no cognitive impairment, and the restrictions arguably discriminate against persons with disabilities and diminish their dignity and autonomy.

Notably, the special needs trust also features a "Medicaid payback provision,"[34] which requires the trust corpus to be used to repay the benefits conferred by the state Medicaid program.[35] In other words, the assets of the individual with a disability will go to the state Medicaid program before any remainder beneficiary, and the payback amount may be so large that a remainder beneficiary would receive nothing from the trust. Certainly, this requirement counters any likely intent of a grantor with a disability. Therefore, the payback requirement often means that this type of trust usually contains only the funds of the person with a disability, such as a personal injury award.[36]

2. *Pooled Special Needs Trusts*

The same challenges of control and direction are also present with pooled special needs trusts. The pooled special needs trust mirrors the individual special needs trust, except that the trust is actually a subaccount of a larger trust established and managed by

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not permitted to establish an OBRA 93 Special Needs Trust personally.").

32. Lawrence Frolik & Melissa Brown, ¶ 17.03[1] *Special Needs Trusts and Personal Injury Settlements*, *in* ADVISING THE ELDERLY & DISABLED CLIENT 4 (2015).

33. *Id.*

34. These trusts are also known as (D)(4)(A) trusts, because of their statutory numbering, or "payback trusts" because of the Medicaid payback provision. Jennifer Field, *Special Needs Trusts: Providing for Disabled Children Without Sacrificing Public Benefits*, 24 J. JUV. L. 79, 87 (2004).

35. 42 U.S.C. § 1396p(d)(4)(A) (noting that "the State will receive all amounts remaining in the trust upon the death of such individual up to an amount equal to the total Medicaid paid on behalf of the individual under a State plan under this subchapter").

36. *See* Frolik & Brown, *supra* note 32, at *1–3. *See generally* John T. Carney, Jr., Comment, *The Defendant Injured Them Once, Don't Let the Government Do It Again: Information and Answers for Protecting Your Medicaid Plaintiffs in a Tort Settlement*, 75 TUL. L. REV. 165 (2000).

a non-profit association[37] to increase management efficiency.[38] The pooled special needs trust does offer more autonomy to the individual with a disability insofar as the individual may establish the trust himself or herself.[39] At first glance, the benefits of efficient management (and reduced cost, by extension) and a degree of autonomy make the pooled special needs trust appear superior to its individual counterpart. After the death of the beneficiary with a disability, the funds remaining in the trust subaccount can be applied to other pooled trust accounts for individuals with disabilities.[40]

Beyond this advantage, the pooled special needs trusts also feature several uncertainties. First, there are different interpretations among the states as to what percentage of the remaining funds can be used for other trust beneficiaries and what percentage must be paid back to the state Medicaid program.[41] Notwithstanding these state differences, the amounts that are not paid out to other trust beneficiaries are, again, paid back to the state's Medicaid program.[42] Second, it is clearly available to persons with a qualifying disability who are under the age of sixty-five, just like the individual special needs trust. However, it is unclear whether it may also be available to persons who are age sixty-five and older.[43] These uncertainties and the added restrictions on

37. 42 U.S.C. § 1396p(d)(4)(C)(i).

38. Johns, *supra* note 28, at 63.

39. 42 U.S.C. § 1396p(d)(4)(C)(iii) (2010) (noting that a subaccount may be established "by the parent, grandparent, or legal guardian of such individuals, *by such individuals*, or by a court." (emphasis added)).

40. Field, *supra* note 34, at 88–89. Because the remainder of the account is first paid to other trust beneficiaries, the trust is sometimes called a "pay-to trust" or a (d)(4)(C) trust due to its statutory numbering. *Id.*

41. *See, e.g.*, MINN. STAT. § 256B.056, subdiv. 3b(d) (2014) ("The retained remainder amount of the subaccount must not exceed ten percent of the account value at the time of the beneficiary's death or termination of the trust."); EDWIN KASSOFF, ELDER LAW AND GUARDIANSHIP IN NEW YORK § 8:131 (2014) (providing that New York allows the beneficiary and the trust management company to negotiate at the time of trust preparation as to the percentage of funds retained). In fact, Pennsylvania used to cap this retention amount at fifty percent, but this provision was later ruled to be pre-empted. Lewis v. Alexander, 276 F.R.D. 421, 444 (E.D. Pa. 2011), *aff'd*, 685 F.3d 325 (3d Cir. 2012).

42. *See* Field, *supra* note 34, at 87–89.

43. *See* 42 U.S.C. § 1396p(d)(4)(C). The interpretation of the age-limit is subject to a circuit-split regarding the countability of assets. The Centers for Medicare and Medicaid Services (CMS) has suggested that states may put age-

remainder beneficiaries mean that pooled special needs trusts are limiting in their own right to individuals with disabilities.

3. Taxation of Special Needs Trusts

In addition to the restrictions of the special needs trusts, there are, of course, taxes. Generally, both individual special needs trusts and pooled special needs trusts are almost always treated as grantor trusts.[44] As such, the income generated from these trusts is taxed at the beneficiary's individual income tax rate.[45] Although this rate is usually low for most public benefit recipients,[46] annual taxes on income can accrue over time, thereby undermining the savings and investment actions taken by the beneficiary or for the beneficiary's benefit.

B. Supplemental Needs Trusts

Naturally, not every individual with a disability has the assets to fund a special needs trust. However, the individual may be surrounded by individuals—perhaps the retirement-ready client mentioned at the beginning of this article—that wish to care for the individual with a disability without disrupting those crucial

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limits on the Medicaid transfer exemption, though not all do. Janet L. Lowder, *Planning for the Disabled or Elderly Client: The Use of Trusts in Disability Benefits Planning*, 23 OHIO PROB. L.J. 5 (2012) (noting that Ohio has not yet recognized an age limit on the transfer exemption); *see also* Lewis v. Alexander, 685 F.3d 325, 344 (3d Cir. 2012) ("We hold that in determining Medicaid eligibility, States are required to exempt any trust meeting the provisions of 42 U.S.C. § 1396p(d)(4)."). However, the Eighth Circuit, construing both federal and North Dakota law, does. *See* Ctr. for Special Needs Tr. Admin., Inc. v. Olson, 676 F.3d 688, 702 (8th Cir. 2012) (finding transfers into trust by those over age sixty-five subject to Medicaid penalty period); *see also* Keith v. Rizzuto, 212 F.3d 1190, 1193 (10th Cir. 2000) ("States accordingly need not count income trusts for eligibility purposes, but nevertheless may . . . opt to do so."); Wong v. Doar, 571 F.3d 247, 256–57 (2d Cir. 2009) ("Congress's negative command that (d)(3) 'shall not apply' to the trusts referenced in (d)(4) does not, however, provide any guidance as to what rules *shall* apply to (d)(4) trusts.").

44. *See* Fleming & Morris, *supra* note 3, at 18–19 (noting that "trusts created by the beneficiaries or by another with the beneficiary's own assets" are almost always treated as grantor trusts).

45. *See id.*; Morris Klein, *The ABLE Act of 2014 Explained!,* PARENTING SPECIAL NEEDS MAG. (Jan. 29, 2015), http://parentingspecialneeds.org/article/new-savings-accounts-may-fund-care.

46. *Id.*

income streams from SSI and Medicaid. In these instances, those relatives or friends may fund a supplemental needs trust for the benefit of the individual with a disability.[47] Like special needs trusts, a supplemental needs trust is a carefully worded discretionary trust with a limited purpose that distributions are "only to supplement and not supplant" public assistance (hence its name).[48] If the supplemental needs trust was established on or after July 1, 1992, then the beneficiary must be disabled at the time the trust is created in order to have the assets excluded for the purposes of Medicaid or SSI eligibility.[49] Additionally, the Social Security Administration suggests in its Program Operations Manual System (POMS) that the trust should be irrevocable, also like the special needs trust, to avoid having assets count toward eligibility.[50] On the up-side, supplemental needs trusts are also not limited by the amount or kind of assets they can hold. As an added benefit, unlike special needs trusts, supplemental needs trusts are not required to include a Medicaid payback provision.[51]

Because supplemental needs trusts are funded with the assets of anyone other than the beneficiary, these kinds of trusts can be useful when elderly parents are using their estate plans to plan for

47. MINN. DEP'T OF HUMAN SERVS., COMBINED MANUAL ch. 15, subdiv. 06.06.03, (2010) http://www.dhs.state.mn.us/main/idcplg?IdcService=GET_DYNAMIC_CONVERSION&RevisionSelectionMethod=LatestReleased&dDocName=cm_0015060603; *accord* MINN. STAT. § 501C.1205, subdiv. (2)(b) (Supp. 2015) ("[A] 'supplemental needs trust' is a trust . . . funded by someone other than the trust beneficiary, the beneficiary's spouse, or anyone obligated to pay any sum for damages or any other purpose to or for the benefit of the trust beneficiary under the terms of a settlement agreement or judgment.").

48. *See* MINN. STAT. § 501C.1205, subdiv. (2)(a); *In re* Leona Carlisle Tr., 498 N.W.2d 260, 265 (Minn. Ct. App. 1993) (providing an example of a supplemental needs trust). The new Minnesota Trust Code specifically excludes supplemental needs trusts from the general prohibition against asset-sheltering trusts. *See* MINN. STAT. § 501C.1205, subdiv. (2)(a).

49. MINN. STAT. § 501C.1205(2)(b); *see* MINN. DEP'T OF HUMAN SERVS., HEALTH CARE PROGRAMS MANUAL ch. 19, subdiv. 25.35.35, http://hcopub.dhs.state.mn.us/hcpmstd/.

50. U.S. SOC. SEC. ADMIN, PROGRAM OPERATIONS MANUAL SYSTEM, § SI 01120.20D [hereinafter POMS], https://secure.ssa.gov/poms.nsf/home!readform (last visited May 9, 2016) (indicating that trusts that can be revoked or terminated by the individual with a disability will be counted as resources for SSI purposes but that trusts that cannot be revoked or terminated and whose assets cannot be directed by the individual with a disability for his or her own support and maintenance will not be counted as resources for SSI purposes).

51. *See generally* MINN. STAT. § 501C.1205.

child with a disability. The purpose they serve is two-fold: (1) to reduce elderly parents' own assets in order to achieve eligibility for Medicaid although a transfer of assets to the trust could arguably be subject to a Medicaid five-year look-back for the elderly parent,[52] and (2) to supplement the Medicaid and SSI their child with disabilities is already receiving. The supplemental needs trust can be a useful planning tool for elderly parents that have substantial assets that are nonetheless insufficient to fund care for both themselves and for their child with disabilities.

While the supplemental needs trust does offer a reprieve from the Medicaid payback, its income tax structure is certainly less favorable than that of a special needs trust. Indeed, income generated from a supplemental needs trust is taxable income, much like the income of the special needs trust.[53] Unlike the special needs trust, however, the supplemental needs trust will be taxed as a "separate taxpayer,"[54] and therefore likely taxed at a higher marginal rate than that of a special needs trust.[55] As a result, the taxation on a supplemental needs trust may slowly diminish the benefit of such trusts.

C. Summary of Special and Supplemental Needs Trusts

In short, special and supplemental needs trusts allow individuals with disabilities to supplement their SSI and Medicaid benefits by sheltering their own assets or the assets of others given for their benefit. However, these tools to shelter assets are not without restriction. While both categories of trusts do not limit the amount or kind of assets that may comprise the trust, these unlimited amounts are well separated from use or direction by the

52. *See generally* MINN. STAT. § 256B.0595 (2014).

53. Fleming & Morris, *supra* note 3, at 18. However, the amount included will be determined based on whether the trust is considered a "complex" or "simple" trust. A complex trust is a non-grantor trust that does not require the distribution of all income to the beneficiary. As such, the amount of taxable income is only the amount actually distributed to the beneficiary. Meanwhile, a simple trust, which requires the distribution of all income to a beneficiary, will have all of its income includable as taxable income. Most supplemental needs trusts will be complex trusts. *Id.*

54. *Id.*

55. Frolik & Brown, *supra*, note 32, at ¶ 17.08[6][a], (noting that the highest marginal rate for trusts is 39.6%); *accord* I.R.C. § 1, subdiv. (e) (2012) (showing the compressed income tax brackets for trusts and estates generally).

individual with a disability. Beyond this, these kinds of trusts are difficult and costly to establish and maintain, and their income is taxable. While these traditional tools of disability planning do offer an individual with a disability greater comfort in that these trusts can pay for certain items that public benefits do not, they are nonetheless limited in their accessibility and applicability, and, by extension, the autonomy they grant the individual with a disability.

III. THE NEW TOOL: THE ABLE ACCOUNT

These limits were at least narrowed with the passage of the ABLE Act in 2014, which created a tax-preferred savings account program specifically for a limited set of "qualified disability expenses." It is important to point out here that the new ABLE accounts are created in the Internal Revenue Code.[56] As such, its regulations will come from the Treasury Department and are therefore focused more on addressing taxation issues and less on SSI or Medicaid eligibility.[57] For guidance of the impact of the ABLE accounts on SSI and Medicaid, the Social Security Administration issued new guidance on March 21, 2016, in the POMS regarding SSI eligibility (and Medicaid eligibility to a limited extent).[58] Though the ABLE Act is perhaps not a perfect solution to the shortcomings of the special and supplemental needs trusts, it does offer some improvements in disability planning in a few key areas: namely greater autonomy for the individual, less complex and less expensive establishment and management, and fewer taxes. Notwithstanding these obvious benefits, the ABLE Act does have a handful of restrictions that reduce the accounts' usefulness, such as age limits, contribution caps, and distribution spending tax disincentives. Still, the new ABLE account does have its place in the disability planner's toolbox.

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56. *See generally* I.R.C. § 529A (Supp. II 2014).

57. Note that the Treasury Department issued proposed regulations in June 2015 that have since gone through the comment period. In response, the Treasury Department has issued interim guidance that shows a handful of changes to the proposed regulations. *See* I.R.S. Notice 2015-81, at 7, https://www.irs.gov/pub/irs-drop/n-15-81.pdf. At the time of this article's printing, the final regulations had not been issued.

58. *See generally* POMS, *supra* note 50, at § SI 01130.740.

A. Generally: Parameters and Restrictions

1. Eligibility: Based on Disability AND Age

ABLE accounts are available only to "eligible individuals," who are:

> (A) entitled to benefits based on blindness or disability under title II or XVI of the Social Security Act, and such blindness or disability occurred before the date on which the individual attained age [twenty-six], or
>
> (B) a disability certification with respect to such individual is filed with the Secretary for such taxable year.[59]

Notably, this disability certification also requires that the "medically determinable physical or mental impairment, which results in marked and severe functional limitations"[60] must have occurred before the individual's twenty-sixth birthday.[61] This cap on age already reveals the limited utility of the new ABLE account. Where supplemental and special needs trusts can be created to deal with a disability that occurred later in life,[62] the new ABLE accounts clearly cannot be used in this way and are therefore better suited to clients planning for known disabilities—either elderly clients who have grandchildren with known disabilities that occurred before the age of twenty-six or younger clients whose children face known disabilities that occurred before the age of twenty-six.

That said, those who are eligible for ABLE accounts are given advantages over beneficiaries of special and supplemental needs trusts. First, unlike these trusts, the ABLE accounts do not need to be established by a parent, grandparent, court-appointed guardian, or by a court hearing. Instead, the individual (or his agent) need only fill out an application from the Department of Human Services (DHS).[63] Therefore, a parent (or a grandparent, or a court-appointed guardian) does not necessarily need to get involved in this process. For those with disabilities, the ease of

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59. I.R.C. § 529A(e)(1). Note that interim guidance from the IRS indicates that this disability certification no longer need be filed. Instead, beneficiaries (or his or her agent) must keep the diagnosis on file and sign under penalty of perjury that they have been thus diagnosed. *See* I.R.S. Notice, *supra* note 57, at 9.

60. I.R.C. § 529A(e)(2)(A)(i)(I).

61. *Id.* § 529A(e)(2)(A)(i)(II).

62. *See supra* Part II.

63. *See, e.g.*, MINN. STAT. § 256Q.05(4) (Supp. 2015).

setting up the account means more than just less work: it means greater autonomy and dignity for the individual with disabilities.

2. *Contribution Freedoms and Limits*

a. *General Limits*

The individual with disabilities can contribute his or her own funds to the ABLE account,[64] like a special needs trust. Similarly, someone other than the beneficiary may also contribute to the ABLE account for the benefit of an individual with disabilities,[65] like a supplemental needs trust. In this sense, the ABLE Act appears to combine the benefits of both of the differently limited special and supplemental needs trusts. On its face, these options appear to impart greater autonomy and flexibility to the individual with a disability.

However, the ABLE Act, like its qualified tuition account counterpart,[66] limits contributions to cash only—a provision that is more limited than special and supplemental needs trusts, which allow contributions of real estate, stock, and many other types of assets.[67] Further, these cash contributions cannot exceed $14,000 a year (the annual gift tax exclusion amount),[68] making these accounts again more limited than both special and supplemental needs trusts, which feature no such ceiling. In fact, $14,000 is the annual limit on *aggregate* contributions from any number of donors.[69] This aggregate limit means that those wishing to support

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64. *See* Qualified ABLE Programs, 80 Fed. Reg. 35,602, 35,614 (June 22, 2015) (to be codified at 26 C.F.R. pts. 1, 25, 26, 301) (capping annual contributions "whether from the designated beneficiary or one or more other persons").

65. *Id.*

66. I.R.C. § 529.

67. *Id.* § 529A(b)(2)(A).

68. *See id.* § 529A(b)(2)(B). This number represents the annual gift tax exclusion as governed by section 2503(b) of the Internal Revenue Code, which is adjusted each year according to the consumer price index. The exclusion for 2015 is $14,000. JOINT COMM. ON TAXATION, GENERAL EXPLANATION OF TAX LEGISLATION ENACTED IN THE 113TH CONGRESS: TITLE I—QUALIFIED ABLE PROGRAMS, 19 (I.R.S.), 2015 WL 1332856, at *4 (Comm. Print 2015).

69. I.R.C. § 529A(b)(2)(B) (applying exclusion amount to "aggregate contributions from all contributors to the ABLE account for the taxable year").

the individual with a disability must coordinate their annual giving to avoid reaching this relatively low ceiling.[70]

Lastly, because an individual can be the beneficiary of only one ABLE account, this aggregate limit truly is a hard annual limit.[71] As a result, this aggregation of contributions means that an elderly client may not be able to simply gift the exclusion amount (as might be done for other grandchildren, children, and other donees) to reduce his or her own estate, for example, if other relatives have already contributed to the maximum annual limit.

Additionally, the ABLE accounts are subject to a $350,000 maximum lifetime cap in Minnesota, although this limit can vary by state.[72] This cap means that a contribution to a child's ABLE account may not even be an option for a client after years of consistent contributions.[73]

b. Means-Tested Limits

i. SSI

Lastly, the SSI payments of the individual with a disability will be suspended when the account balance, including earnings on contributions, reaches $100,000.[74] As section 103(a)(1) of the ABLE Act states,

> Notwithstanding any other provision of Federal law that requires consideration of [one] or more financial

70. For tax consequences of contributions in excess of the yearly amount, see *infra* Section III.B.1.a.

71. I.R.C. § 529A(b)(1)(B).

72. *Id.* § 529A(b)(6) (prohibiting aggregate contributions to the amount set under the qualified tuition accounts in section 529(b)(6)). This amount does *not* include the earnings on the contributions. Qualified ABLE Programs Regulations, 80 Fed. Reg. 35,602, 35,612 (June 22, 2015). The new Minnesota Statutes section 256Q.06, subdivision 2 provides that the limit on this aggregate amount is based on Minnesota Statutes, section 136G.09, subdivision 8, which in turn provides that the Minnesota Office of Higher Education shall establish this amount. Currently, this amount is set to $350,000. *See* MINN. COLL. SAV. PLAN, COMPARE COLLEGE SAVINGS CHOICES 3, https://www.mnsaves.org/documents/mn_compare.pdf (last visited May 4, 2016).

73. Theoretically, an ABLE account would reach this limit after twenty-five years of contributions at the full gift tax exclusion amount. This eventuality is a future hypothetical that elder law attorneys could not expect to encounter until at least twenty-five years from now.

74. I.R.C. § 529A notes (a)–(b) (Treatment of ABLE Accounts Under Certain Federal Programs).

> circumstances of an individual, for the purpose of determining eligibility to receive, or the amount of, any assistance or benefit authorized by such provision to be provided to or for the benefit of such individual, any amount (including earnings thereon) in the ABLE account (within the meaning of section 529A of the Internal Revenue Code of 1986) of such individual, any contributions to the ABLE account of the individual, and *any distribution for qualified disability expenses (as defined in subsection (e)(5) of such section) shall be disregarded for such purpose with respect to any period during which such individual maintains, makes contributions to, or receives distributions from such ABLE account,* except that, in the case of the supplemental security income program under title XVI of the Social Security Act—
>
> (1) a distribution for housing expenses (within the meaning of such subsection) shall not be so disregarded . . . ."
>
> *(2) in the case of such program, any amount (including such earnings) in such ABLE account shall be considered a resource of the designated beneficiary to the extent that such amount exceeds $100,000.*[75]

Note that housing expenses still have the potential to the trigger an SSI suspension[76] (housing expense distribution rules will be discussed more fully in Section III.A.3). According to the new POMS section on the ABLE Act, suspension occurs as a result of including account balances in excess of $100,000 as part of the individual's countable *resources*,[77] not income. In fact, no contributions to the ABLE account or the account's earnings are to be counted as income.[78] The disregard of income here indicates that the Social Security Administration is generally not looking to reduce SSI payments by treating ABLE account distributions as income, but rather it seeks to determine eligibility by treating excess contributions to the ABLE account as a countable resource.

Even so, these restrictions do mean that contributions to an ABLE account, while perhaps well-intentioned, may result in the loss of the beneficiary's SSI benefits. Therefore, contributions to an

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75. *Id.* § 103(a) (emphasis added).
76. *Id.* § 103(a)(1).
77. POMS, *supra* note 50, at §§ SI 01130.740.C.5, .D.
78. *Id.* §§ SI 01130.740.C.1–.C.2.

ABLE account from a donor must be carefully analyzed in the context of any amounts already contributed to the account.

ii. Medicaid

Sometimes, the loss of the relatively small SSI payments may not be the primary concern to some individuals with disabilities. They may instead be more concerned about their Medicaid benefits, which can be generous and essential to living with their disabilities. Fortunately, both the ABLE Act itself and the POMS are highly permissive when it comes to Medicaid eligibility. Section 103(b)(2) of the ABLE Act states,

> An individual who would be receiving payment of such supplemental security income benefits but for the application of paragraph (1) [in which SSI is suspended for excess resources] shall be treated for purposes of title XIX of the Social Security Act as if the individual continued to be receiving payment of such benefits.[79]

As title XIX of the Social Security Act concerns itself with Medicaid,[80] the wording of the ABLE Act indicates that SSI-based Medicaid will be unaffected by an SSI suspension due to excess ABLE account balances. The POMS appears to track with the federal law in applying this special rule.[81] These rules mean that ABLE account holders have a choice about how they wish to handle contributions: whether to allow the account balance to exceed $100,000 thereby suspending his or her SSI payments while still retaining Medicaid. While this feature is not immediately useful, it should be carefully considered when deciding which disability planning tools to use. For certain individuals with disabilities, this choice may be very appealing.

3. Investment and Distribution Limits

The investment and use of the money in the ABLE account is also limited. First, the beneficiary of the ABLE account (i.e., the individual with a disability)[82] can direct the investment of

79. ABLE Act § 103(b)(2).

80. *See Compilation of the Social Security Laws: Title XIX—Grants to States for Medicaid Programs*, U.S. SOC. SECURITY ADMIN., https://www.ssa.gov/OP_Home/ssact/title19/1900.htm (last visited Apr. 18, 2016).

81. POMS, *supra* note 50, at § SI 01130.740.D.1.a.

82. I.R.C. § 529A(e)(3) (Supp. II 2014) (defining "designated beneficiary" as

contributions only twice per year.[83] Also, monies held in these accounts cannot be used as security for a loan.[84] Most importantly, distributions to the beneficiary—in order to avoid taxation—must be made towards "qualified disability expenses."[85] Notably,

> 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 personal 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.[86]

These expenses are similar to the kinds of expenses paid for by a discretionary supplemental needs or special needs trust with the major exception that ABLE accounts do not appear to allow the type of non-disability-related, quality-of-life enhancing purchases that are allowed by supplemental and special needs trusts, such as entertainment and travel. Unlike these trusts, however, the ABLE Act's proposed regulations do not appear to limit these disability expenses to "supplemental" needs.[87] The proposed regulations do indicate that distributions made for housing expenses will be counted against the beneficiary's SSI eligibility,[88] which is true for

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the eligible disabled individual).

83. *Id.* § 529A(b)(4).

84. *Id.* § 529A(b)(5).

85. *Id.* § 529A(c)(1)(B).

86. *Id.* § 529A(e)(5).

87. Qualified ABLE Programs Regulations, 80 Fed. Reg. 35,602, 35,612 (June 22, 2015) (to be codified at 26 C.F.R. § 1.529A-2(h)(1)) ("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.").

88. *Id.* (to be codified at 26 C.F.R. § 1.529A-2(h)(1)) ("A qualified ABLE program must establish safeguards to distinguish between distributions used for the payment of qualified disability expenses and other distributions, and to permit the identification of the amounts distributed for housing expenses as that term is defined for purposes of the Supplemental Security Income program of the Social Security Administration."); *accord* I.R.C. § 529A note (a)(1). Note that proposed IRS regulations dropped this requirement, which had originally been part of the proposed regulations in an effort to track housing expenses for SSI program

supplemental and special needs trusts as well.[89] However, as a general rule, distributions will not be counted as *income* by the Social Security Administration for SSI eligibility purposes,[90] with the exception of housing-related distributions.[91] Instead, such distributions will count as resources under specific rules as outlined below.

Generally, the POMS allows an individual to retain distributions for non-housing qualified disability expenses beyond the month of distribution without counting them as resources (and therefore suspending SSI benefits) as long as the individual maintains an ABLE account, does not spend the distribution, keeps the ABLE money "identifiable,"[92] and still intends to use the retained funds for a qualified disability expense.[93] If the individual's intent changes or the individual spends the distribution on a non-qualified disability expense, then the amount spent will be a countable resource as of the first of the month in which the funds were spent or the intent of the individual changed.[94]

What these retention rules mean is that, theoretically, an individual could take a distribution from the ABLE account and place the funds in another account (i.e., a checking account or perhaps even a university card for education purchases made on campus) and not have the unspent balance count as resources as long as the individual still intended to use the funds for a non-housing qualified disability expense.[95]

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eligibility. However, after the comment period, the Treasury Department noted that, because this housing delineation would not affect taxation (which is the subject matter of its regulations generally), the requirement would be deleted from the final regulations. *See* I.R.S. Notice, *supra* note 57, at 4.

89. *See* POMS, *supra* note 50, at §§ SI 00835.200–.310 (linking the "one-third reduction rule" to in-kind income which may come by way of trust).

90. *Id.* § SI 01130.740.C.4.

91. I.R.C. § 529A note (a)(1).

92. Note, however, that the Social Security Administration does have rules for tracing comingled funds that state physical separateness of funds is not required but that non-excluded funds are always considered withdrawn first from comingled accounts. *See generally* POMS, *supra* note 50, at §§ SI 01130.700.A–.B.

93. *Id.* § SI 01130.740.C.5.a.

94. *Id.* § SI 01130.740.D.3.

95. The standard for intent is not clear. However, the Social Security Administration offers the following example as showing a change in intent:

> In June, Jennifer takes a $7,000 distribution from her ABLE account to pay her college tuition—a QDE. Her tuition payment is due in September. In August, Jennifer gets a job offer and decides not to

Further, non-housing related ABLE account distributions that are spent within the same month of their distribution are also not counted as income or resources, regardless of whether they are qualified disability expenses.[96] This rule means that an ABLE account beneficiary can spend an ABLE distribution on a non-qualified purchase without having it count as a resource for SSI purposes if the spending occurs within the same month of the distribution—though such a beneficiary may be exposed to taxation for such spending.[97] In any event, the general structure of these rules indicates that the Social Security Administration is willing to engage in relatively permissive resource counting regarding distributions from an ABLE account, except for housing-related expenses.

In contrast, the POMS rules on ABLE accounts are less flexible in regard to housing expenses, as indicated by the separate consideration of housing expenses in section 103 of the ABLE Act itself. Housing-related qualified disability expenses must be spent in the month they are distributed to avoid being counted as resources.[98] Therefore, the beneficiary is probably safest to have a distribution made directly to the housing vendor, if possible.

That is, the POMS tracks with the ABLE Act itself: not counting as resources non-housing-related distributions and counting housing-related distributions. Not counting distributions as income or resources does make inroads toward greater

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> return to school. Since she no longer intends to use it for tuition, the $7,000 becomes a countable resource in September unless Jennifer redesignates it for another QDE or returns the funds to her ABLE account prior to September.

Id. § SI 01130.740.D.3.c.

96. *Id.* § SI 01130.740.D.2.

> Count a distribution for a housing-related QDE *or for an expense that is not a QDE* as a resource, if the beneficiary retains the distribution into the month following the month of receipt. *If the beneficiary spends the distribution within the month of receipt, there is no effect on eligibility.* However, apply normal SSI resource counting rules and exclusions to assets or other items purchased with funds from an ABLE account.

Id. (emphases added). Section SI 01130.740.D.3, which counts non-qualified disability expenses as resources, applies specifically to *retained* distributions, not those spent within the month of their receipt. Therefore, normal SSI resource rules apply to the item purchased with the ABLE funds (for example, if a second car is purchased, then it would count as a resource).

97. *See infra* Section III.B.1.b.

98. POMS, *supra* note 50, at § SI 01130.740.D.2.

autonomy and dignity for an individual with disabilities compared with the restrictions of the special and supplemental needs trusts. However, it is important to note that the beneficiary of a Minnesota ABLE account must first *request* the distribution,[99] so the ABLE account should not be misconstrued as a typical checking account. Instead, at least in Minnesota, the ABLE account exists as a "separate trust" in the state treasury.[100] That is, the relative freedom from means-testing with an ABLE account is circumscribed by its own administrative hurdles.

These hurdles aside, the beneficiary is the only person who has the authority to request distributions,[101] and these distributions "may be made:"

> (1) directly to participating providers of goods and services that are qualified disability expenses, if purchased for the beneficiary;
> (2) in the form of a check payable to both the beneficiary and provider of goods or services that are qualified disability expenses; or
> (3) directly to the beneficiary, if the beneficiary has already paid qualified disability expenses.[102]

The beneficiary may distribute funds to himself or herself.[103] The ABLE account is much more flexible than the supplemental or special needs trusts which prohibit distributions from being made directly to the beneficiary and, again, affords the beneficiary more autonomy and dignity. While affording the beneficiary more autonomy compared to a trust, the ABLE Act also imposes additional responsibilities on the beneficiary by requiring detailed

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99. MINN. STAT. § 256Q.06, subdiv. 3 (Supp. 2015).

100. *Id.* § 256Q.06, subdiv. 5 ("All assets of the plan, including contributions to accounts, are held in trust for the exclusive benefit of account owners. Assets must be held in a separate account in the state treasury to be known as the Minnesota ABLE plan account or in accounts with the third-party provider . . . .").

101. MINN. STAT. § 256Q.06, subdiv. 3.

102. *Id.* § 256Q.08, subdiv. 1. Also, the last method of distribution directly to the beneficiary is a *huge* advantage of the ABLE account over the traditional special or supplemental needs trust. In either of these trusts, payments can never be made directly to the beneficiary. This set up often leads to frustration and reduces the disabled individual's sense of dignity because he is not in control of his own money—by virtue of the trustee directly paying third-party vendors instead of permitting this autonomy in the individual with a disability.

103. *Id.* § 256Q.08, subdiv. 3.

record keeping and administration in strict compliance with the ABLE Act's tax regulations.[104]

B. *Taxation and Accountability*

1. *Taxation*

As stated previously, the ABLE Act is primarily a tax law (with the exception of the suspension of SSI benefits for cumulative account balances greater than $100,000 and/or housing expenses that are considered countable resources if not spent within the month of the distribution's receipt and the special Medicaid retention rule).[105] As a result, (if SSI eligibility were not the primary concern) the penalties for exceeding contribution limits or taking non-qualified distributions is taxation.

a. *On Excess Contributions*

First, the beneficiary is subject to an excise tax of six percent on contributions exceeding the annual gift tax exclusion that are *also* not returned (along with any accrued earnings) to the contributor during the taxable year.[106] By law, the state "must return excess . . . contribution[s][107] or excess aggregate

104. *See infra* Section III.B.2.

105. I.R.C. § 529A note (a)(2) (Supp. II 2014). It is important to note that this $100,000 aggregate account balance cap suggests that a beneficiary could theoretically contribute over $14,000 in one year (i.e., in a personal injury settlement) and still be eligible for SSI benefits, as long as that contribution did not make the total account balance exceed $100,000. However, it seems that the state ABLE program would attempt to send the excess back to the contributor (or out of the account), as the state is entrusted with ensuring that these yearly limits are honored and not taxed. *See infra* Section III.B.2. Although, theoretically, it is possible that a personal injury settlement could be placed in the account and the beneficiary would simply pay the excise tax and still maintain eligibility for SSI under $100,000, the practical workings of this solution are still unclear.

106. THE ARC, ACHIEVING A BETTER LIFE EXPERIENCE (ABLE) ACT: DIVISION B OF PUBLIC LAW 113-295, DECEMBER 19, 2014, at 1, 4 (2015), http://www.thearc.org/document.doc?id=5009&erid=6420135 (citing I.R.C. § 2503(b) (2012)); *accord* MINN. STAT. § 256Q.08, subdiv. 3; *see also* Qualified ABLE Programs Regulations, 80 Fed. Reg. 35,602, 35,612 (June 22, 2015) (to be codified at 26 C.F.R. § 1.529A.-3(d)).

107. Contributions exceeding over $14,000 annually under the gift tax exclusion of I.R.C. § 2503(b).

contribution[s][108] . . . to the person or persons who made that contribution."[109] Therefore, the imposition of this "excess contribution" tax is unlikely to occur since the state must return an excess contribution to the contributor.[110] Based on these regulations, it appears that the onus is on the state to categorize and manage contributions, which should ultimately prevent the beneficiary from getting taxed on excess contributions. In fact, commenters on the proposed regulations "expect that most qualified ABLE programs will adopt the infrastructure currently utilized by state [section] 529 qualified tuition programs either to reject such excess contributions or to escrow and immediately refund the excess contributions."[111] Therefore, there is at least some consensus that excess contributions will be unlikely, as will the resulting tax on earnings of those contributions.[112] Taking the analysis a step further, this safeguard also means that the ABLE Act

108. Contributions over $350,000 to the ABLE account in total. *See* Qualified ABLE Programs, 80 Fed. Reg. at 35,614.

109. *Id.*

110. I.R.C. § 529A(b)(6) (Supp. II 2014) (requiring the state ABLE program to provide "adequate safeguards to prevent aggregate contributions on behalf of a designated beneficiary in the excess of the limit established"). The proposed Treasury regulations provide,

> To implement these requirements, the proposed regulations provide that a qualified ABLE program must return contributions in excess of the annual gift tax exclusion (excess contributions) to the contributor(s), along with all net income attributable to those excess contributions. Similarly, the proposed regulations also require the return of all contributions, along with all net income attributable to those contributions, that caused an ABLE account to exceed the limit established by the State for its qualified tuition program (excess aggregate contributions). If an excess contribution or excess aggregate contribution is returned to a contributor other than the designated beneficiary, the qualified ABLE program must notify the designated beneficiary of such return at the time of the return. The proposed regulations further provide that such returns of excess contributions and excess aggregate contributions must be received by the contributor(s) on or before the due date (including extensions) of the designated beneficiary's income tax return for the year in which the excess contributions were made or in the year the excess aggregate contributions caused amounts in the ABLE account to exceed the limit in effect under section 529A(b)(6), respectively.

Qualified ABLE Programs, 80 Fed. Reg. at 35,606; *see id.* at 35,614 (to be codified at 26 C.F.R. § 1.529A-2(g)(4)).

111. I.R.S. Notice, *supra* note 57, at 7.

112. *See id.*

might not be the most appropriate vehicle for a personal injury award, unless the settlement is structured to meet the ABLE account's contribution limits. Of course, we may learn more when the state program releases its implementing rules.[113]

b. On Non-Qualified Distributions

The proposed regulations originally provided that the state ABLE program[114] "must establish safeguards to distinguish between distributions used for the payment of qualified disability expenses and other distributions."[115] However, interim guidance from the IRS states that, due to comments received during the comment period, this burden will shift to the ABLE account holder.[116] In any event, each distribution is a portion of the investment and the earnings.[117] Because this combination resembles the pay-outs on annuities, the amount includable in gross income is only the earnings portion (as calculated pursuant to the exclusion ratio of section 72 of the Internal Revenue Code)[118] that exceeds the amount of "qualified disability expenses."[119] That is, if the disability expenses are twenty-five dollars and the distribution requested by the beneficiary is twenty-five dollars, then the beneficiary includes none of the distribution in her gross income.[120] If, however, the disability expenses are twenty-five dollars and the distribution requested by the beneficiary is fifty dollars, then the beneficiary would include as gross income only the earnings portion of the

113. DHS is currently working with fifteen other states in a collaborative implementation effort. The new plans—and likely their regulations—are expected to roll out in late 2016. *See* MINN. DEP'T HUMAN SERVS., DISABILITY SERVS. DIV., MINNESOTA ABLE ACT UPDATE: DECEMBER 11, 2015, at 1 (2015) [hereinafter ABLE ACT UPDATE], http://www.thearcofminnesota.org/wp-content/uploads/2015/12/ABLE-Update-from-MN-DHS-12.11.15.pdf.

114. *See infra* Section III.B.2 (regarding how the state actually runs the ABLE program).

115. Qualified ABLE Programs, 80 Fed. Reg. at 35,615. Note, however, that, under the final regulations, the state ABLE program will not be monitoring distributions.

116. *See infra* notes 132, 133 and accompanying text.

117. Qualified ABLE Programs, 80 Fed. Reg. at 35,615; *see* I.R.C. § 529A(c)(B) (Supp. II 2014).

118. *See generally* I.R.C. § 72 (2012).

119. Qualified ABLE Programs, 80 Fed. Reg. at 35,615. For full definition of "qualified disability expenses," see *supra* Section III.A.3

120. *See* Qualified ABLE Programs, 80 Fed. Reg. at 35,615.

distribution.[121] In determining the final amount of includable distributions, all of the excess distributions are aggregated over the course of the taxable year.[122] These excess contributions are then taxed at the beneficiary's taxable rate plus ten percent.[123] Notwithstanding this tax, the Minnesota ABLE Act further clarifies that such non-qualified distributions can be requested "*at any time*," seemingly without an additional consequence beyond the tax.[124]

In contrast to either a special needs or supplemental needs trust, the ABLE account does offer tax-preferred savings, as long as the distributions are used for qualified disability expenses. This insulation from taxation is one of the advantages of an ABLE account compared to special and supplemental needs trusts. However, because the amount of contributions to the ABLE accounts are constrained by law and therefore accrue more slowly, this tax advantage is a limited one. Therefore, the tax savings of these accounts may actually be smaller than anticipated.

2. *Reporting Mechanisms*

ABLE accounts are housed under a much larger state-run "ABLE plan."[125] Specifically, the State of Minnesota carries out the administration and investing of these ABLE accounts.[126] In fact, the administrative onus appears to be on the state ABLE plan. As noted above, the state "must return . . . excess contribution[s]"[127] "or excess aggregate contribution[s]"[128] "to the person or persons who made [the] contribution."[129] The final version of the regulations

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121. *See id.*
122. *See id.*
123. *See id.* at 35,616.
124. *See* MINN. STAT. § 256Q.08, subdiv. 3 (Supp. 2015) (emphasis added).
125. *See* I.R.C. § 529A(b)(1), (e)(6) (Supp. II 2014).
126. *See, e.g.*, MINN. STAT. § 256Q.05, subdiv. 5 (authorizing DHS to charge a fee for administration); *id.* § 256Q.05, subdiv. 6 (requiring DHS to submit notices to both the IRS and the beneficiary of the ABLE account); *id.* § 256Q.07, subdiv. 1 (authorizing the State Board of Investment to invest the cash in the ABLE accounts); Qualified ABLE Programs Regulations, 80 Fed. Reg. 35,602, 35,616–19 (June 22, 2015) (directing the manner in which records will be kept and submitted by the states).
127. Contributions exceeding over $14,000 annually. *See* I.R.C. § 2503(b) (2012) (gift tax exclusion); Qualified ABLE Programs, 80 Fed. Reg. at 35,612, 35,614 (defining excess contribution).
128. *Id.* (defining excess aggregate contribution).
129. *Id.* at 35,614.

will not require the state ABLE program to collect the tax identification numbers of all contributors; instead a tax identification number will be required only for those taxpayers that make excess contributions or excess aggregate contributions.[130]

Note, however, that administrative responsibilities appear to be shifting as the ABLE Act is implemented. According to interim guidance from the IRS issued near the end of 2015, the state ABLE program will not be required to provide safeguards that distinguish between qualified disability expenses and other expenses.[131] Instead, for federal tax purposes, the beneficiary (or an agent thereof) must track these expenses himself or herself in case of audit.[132]

C. *Medicaid Payback Provision*

Much like an individual special needs trust,[133] the remainder of the funds in ABLE accounts when the beneficiary dies are subject to recovery by Medicaid to the extent that Medicaid paid for the beneficiary's medical expenses while the account was in effect.[134] Internal Revenue Code, section 529A(f) states:

> Subject to any outstanding payments due for qualified disability expenses, upon the death of the designated beneficiary, all amounts remaining in the qualified ABLE account not in excess of the amount equal to the total Medicaid paid for the designated beneficiary after the establishment of the account, net of any premiums paid from the account or paid by or on behalf of the beneficiary to a Medicaid Buy-In program under any State Medicaid plan established under title XIX of the Social Security Act, shall be distributed to such State upon filing of a claim for payment by such State. For purposes of this paragraph, the State shall be a creditor of an ABLE account and not a beneficiary . . . .[135]

Therefore, every ABLE account is subject to a Medicaid payback, and the planning available with a third-party supplemental needs trust—to avoid the payback—is not available

130. I.R.S. Notice 2015-81, *supra* note 57, at 4.
131. *Id.* at 7.
132. *See id.* at 4–5; ABLE ACT UPDATE, *supra* note 113, at 2.
133. *See supra* Section II.A.3.
134. Brogan et al., *supra* note 8, at 43.
135. I.R.C. § 529A(f) (Supp. II 2014).

for ABLE act accounts, even if the funds in the account are contributed by a third-party.

Even so, the amount paid back to Medicaid is *not* considered a taxable distribution.[136] Additionally, this amount is only to be paid after outstanding debts for qualified disability expenses have been paid.[137] Therefore, while the amount remaining in the ABLE account is includable in the gross estate of the beneficiary at death, both qualified disability vendors and Medicaid, are treated as creditors, such that these claims may be deductible against the gross estate.[138] Further, because "qualified disability expenses" include funeral and burial expenses, the proposed regulations suggest that distributions for these expenses can be paid before the state recovers any Medicaid payments.[139] This priority is a significant improvement, and more humane, than the payback rules for special needs trusts, which do not allow for the payment of funeral and burial expenses before reimbursing the state.[140]

Notwithstanding this Medicaid payback provision and the estate tax implications, an ABLE Act beneficiary may rollover portions of his or her account to a family member who has a disability—and who is eligible under the ABLE Act—or may simply

136. Qualified ABLE Programs Regulations, 80 Fed. Reg. 35,602, 35,609 (June 22, 2015) (to be codified at 26 C.F.R. § 1.529A-2(p)); *accord* I.R.C. § 529A(f) (Supp. II 2014).

137. Qualified ABLE Programs, 80 Fed. Reg. at 35,609.

138. *See id.* at 35,609, 35,616 (to be codified at 26 C.F.R. §§ 1.529A-3(b)(4), 1-4(d)) ("Upon the death of the designated beneficiary, the designated beneficiary's ABLE account is includable in his or her gross estate for estate tax purposes under section 2031. The payment of outstanding qualified disability expenses and the payment of certain claims made by a State under its Medicaid plan may be deductible for estate tax purposes if the requirements of section 2053 are satisfied.").

139. *Id.* at 35,615 (to be codified at 26 C.F.R. §1.529A-3(p) (requiring that the "payment of [a Medicaid recovery] (if any) will be made only after providing for the payment from the designated beneficiary's ABLE account of all outstanding payments due for his or her qualified disability expenses"); *id.* at 35,614 (to be codified at 26 C.F.R. § 1.529A-3(h)(1) (including "funeral and burial expenses" in definition of "qualified disability expenses"); *accord* I.R.C. § 529A(e)(5) (Supp. II 2014).

140. POMS, *supra* note 50, at § SI 01120.203.B.3.b (providing that funeral expenses will not be permitted before the Medicaid lien is paid); *see also* Kristen M. Lewis, Am. Bar Ass'n, *Special Needs Trusts: The Cornerstone of Planning for Beneficiaries with Disabilities*, *in* SPECIAL NEEDS TRUSTS BASICS 27 (2010) (noting that burial and funeral expenses that have not been pre-paid before death will not be paid by the special needs trust until after the Medicaid lien has been satisfied).

change the designated beneficiary to such individual.[141] In fact, such a transfer during life is exempt from both gift tax and generation-skipping transfer tax.[142]

D. *When Available to Minnesota's Individuals with Disabilities*

The ABLE Act authorizes states to implement and manage ABLE accounts.[143] Accordingly, Minnesota Governor Mark Dayton signed Minnesota's ABLE Act into law on May 22, 2015,[144] with an effective date of July 1, 2015.[145] Minnesota's version authorizes the Minnesota DHS to "establish rules, terms, and conditions" for the new ABLE accounts and to "prescribe the applications forms, procedures, and other requirements that apply to the plan."[146]

The Minnesota DHS expects the new ABLE Act plans to be available in late 2016.[147] The roll-out of the new plans may actually precede the final regulations from the Treasury Department. However, anticipating the plodding rulemaking process, the Treasury Department has explicitly stated that states operating ABLE programs, along with their beneficiaries, will still receive favorable tax status during the interim even if their programs do not fully comport with the final regulations.[148]

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141. *See* I.R.C. § 529A(c)(1)(C)(1)–(2) (Supp. II 2014) (exempting from taxation the distributee of any such rollover). Theoretically, the Medicaid payback could be avoided if the beneficiary changed the designated beneficiary on his ABLE account to a qualified family member before his death. However, this theory has obviously not been tested and this course of action should be advised with caution; for all planning lawyers, untested theories mean possible litigation and increased expense for the client (and his or her beneficiaries by extension). Moreover, beneficiaries may not have another family member with a disability that appeared before age twenty-six that could become the new designated beneficiary. As a result, this option is not available to everyone.

142. Qualified ABLE Programs, 80 Fed. Reg. at 35,616 (to be codified at 26 C.F.R. § 1.529A-4(c)).

143. THE ARC, *supra* note 106, at 6.

144. *Status of S.F. 1458*, MINN. ST. LEGISLATURE, https://www.revisor.mn.gov/bills/bill.php?b=senate&f=sf1458&ssn=0&y=2015 (last visited May 4, 2016).

145. S.F. 1458, §§ 44–51 (codified as amended at MINN. STAT. §§ 256Q.01–.08), 2015 Leg., 89th Sess. (Minn. 2015), https://www.revisor.mn.gov/bills/text.php?number=SF1458&version=3&session=ls89&session_year=2015&session _number=0; *see also* MINN. STAT. § 256Q.05, subdiv. 1 (Supp. 2015).

146. *Id.* § 48 subdiv. 2(a)–(b) (codified as amended at MINN. STAT. § 256Q.05, subdiv. 2(a)–(b) (Supp. 2015)).

147. ABLE ACT UPDATE, *supra* note 113, at 2.

148. Qualified ABLE Programs, 80 Fed. Reg. 35,602, 35,604 (June 22, 2015)

IV. CONCLUSION

ABLE accounts have some advantages over special and supplemental needs trusts because they avoid taxes on earnings that the accounts accrue. They also generally avoid the often costly attorney-intensive establishment of such trusts. However, the biggest benefit of this new tool may well be the independence and dignity they afford people with disabilities: the new ABLE accounts empower individuals with disabilities to establish, fund, direct investments, and request withdrawals from the account on their own. By contrast, the special and supplemental needs trusts take control out of the hands of individuals with disabilities and must be established by often complex court proceedings that are difficult to understand without the help of an attorney. Also, ABLE accounts allow anyone, including the beneficiary, to contribute to the beneficiary's needs without affecting his or her SSI and Medicaid (subject to the $100,000 account balance SSI suspension limit).

On the flip side, the POMS rules on ABLE accounts inject their own kind of complexity for tracking housing-expenses and non-qualified disability expenses and ensuring that those distributions are spent within the month of their receipt. However, the POMS rules offer a number of features that really stand to increase autonomy and quality of life: the exclusion of both contributions and distributions from income for SSI purposes, the exclusion from resources of retained distributions for non-housing qualified disability expenses under certain circumstances, and even the exclusion from resources of housing-related qualified disability expenses and *non-qualified* disability expenses if the distribution is spent within the month of receipt. Additionally, the option to exceed the $100,000 SSI limit on the total account amount while still retaining Medicaid benefits is a huge advantage for individuals with disabilities who are willing to forego SSI but still want the benefits of Medicaid coverage.

Yet, these benefits are significantly mitigated because contributions are capped, and eligibility is limited to those with a disability that began before age twenty-six. As a result, the ABLE accounts are possible solutions mainly for three types of clients: (1) elderly clients who have family or friends who are qualifying beneficiaries with a disability; (2) younger clients who wish to plan

(to be codified at 26 C.F.R. § 1.529A-4(c)).

for their child with disabilities; or (3) adults with a disability that began before age twenty-six who prefer the advantages of an ABLE account.

Because of the age limit and contribution limits, ABLE accounts will not replace the need for special and supplemental needs trusts for many people. However, under the right circumstances, ABLE accounts will be effective, either instead of, or in addition to, the planning available through special and supplemental needs trust. In short, the ABLE account is a welcome addition to the disability planner's tool-box, but it is only one tool that can maximize planning.