Key Wealth Institute

Safeguarding the Future: A Guide to Special Needs Trusts and Pooled Special Needs Trusts

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Navigating the labyrinth of financial planning for individuals with special needs requires a balance of foresight, legal expertise, and familial care. Special needs trusts (SNTs) and pooled special needs trusts (PSNTs) lie at the heart of this journey. These tools are designed to deal with the complexities of disability finance.

As families weigh their options, they need to understand the distinctions and benefits of both to secure a stable and enriched future for their loved ones.

Families often learn that Medicaid or Supplemental Security Income (SSI) do not provide for clothing, travel, equipment for sports or hobbies, or certain health services. If the SNT or PSNT is set up properly, it can fund these extras without supplanting the government benefits.

Three players perform vital roles in the success of both kinds of trusts.

The grantor, often the parent, grandparent or other relative or friend, initiates the trust by infusing it with assets ranging from cash to real estate.

The trustee is central to the trust's operational machinery. This person or organization is empowered to manage the trust's assets, make astute investment decisions, and execute distributions according to the trust document's directives.

These gestures set the stage for securing the financial well-being of **the beneficiary,** the individual with special needs who benefits from the trust's resources.

A Blueprint for Charting your Course

The trust document provides a blueprint for the operational framework of a special needs or pooled special needs trust. The document contains the distribution guidelines, charting the course for strategic fund allocations to enhance the beneficiary's quality of life while preserving their eligibility for government benefits.

The document outlines permissible investment strategies for the trust's assets, ensuring the trustee adheres to a risk management approach suitable for the trust's goals and long-term needs.

The trust document also defines a clear path for the trust's future if the primary trustee becomes incapacitated or dies. A successor trustee is nominated to seamlessly take over the responsibilities and continue managing the trust to ensure the beneficiary's well-being.

Which Type of SNT Is Best for You?

There are two distinct types of special needs trusts:

- First-party or self-settled SNT
- Third-party SNT

The beneficiary funds the former, which poses unique challenges, with stricter qualification criteria for government benefits.

In a self-settled SNT, the assets used to create the trust belong to the beneficiary. The funding might be from money they've earned or received as an inheritance or a personal injury settlement.

However, self-settled SNTs typically have stricter rules about eligibility for government benefits such as Medicaid and SSI because the beneficiary originally owned the assets in the trust.

Section 1396p(d)(4)(A) of the Social Security Act allows for a special type of self-settled SNT. A d4A trust offers some flexibility regarding Medicaid eligibility if certain criteria are met, usually that the beneficiary became disabled before reaching a certain age (often 65).

An important aspect of d4A trusts is the payback provision: Upon the beneficiary's death, Medicaid can claim reimbursement from the remaining trust assets for benefits provided. However, any funds left after reimbursing Medicaid can be distributed according to the trust document's stipulations.

In contrast, third-party SNTs, fueled by contributions from external sources such as parents, grandparents, and other relatives or friends, often provide much more financial stability for the beneficiary.

Since the beneficiary doesn't own a third-party trust, its assets won't disqualify them from receiving Medicaid or SSI. The grantors can use a third-party SNT to ensure their loved one with special needs receives financial security even after the grantors are gone.

There's also no requirement to reimburse Medicaid from the third-party trust upon the beneficiary's death.

Consulting with an attorney who specializes in SNTs is vital to determine whether self-settled or third-party trusts are the most suitable option. The attorney can ensure the trust is created following legal guidelines in your state to maximize its benefits.

However, it is important to note that establishing and managing an individual SNT has its drawbacks. The initial set-up costs involving lawyers and financial advisors can be significant. Additionally, ongoing administrative fees can strain the trust's resources. This is particularly true for families with limited financial means.

Another Option: The Pooled Special Needs Trust

Pooled special needs trusts (PSNTs) offer a compelling alternative.

As the name suggests, a PSNT combines resources from multiple beneficiaries and is managed by a nonprofit organization that is a qualified 501(c)(3). The nonprofit has fiduciary responsibility, ensuring the funds are used solely for the trust's beneficiaries. PSNTs benefit from economies of scale, allowing for reduced administrative costs and access to better investment opportunities compared to individual trusts.

Each beneficiary of a PSNT has an individual account, but the funds are invested collectively. The earnings are then distributed proportionately based on the amount in each individual's account. This collective investment strategy helps in achieving higher returns and diversifies the investment risks.

Establishing a PSNT with a qualified nonprofit is not difficult or expensive. During the enrollment meeting with the nonprofit, the family would complete a joinder or contribution agreement — a document that dictates the trust's participant terms. The easy set-up allows families to secure financial stability quickly for their loved ones. Funds in a PSNT are pooled together for administrative efficiency and investment optimization, allowing for better management and potential growth of the assets.

A certain type of PSNT, often referred to as an excess income trust, allows the beneficiary to earn income without losing Medicaid benefits and to pay for living expenses. An excess income trust works well for employed people with disabilities and retired seniors who need support at home.

PSNTs offer several other benefits, including:

Cost-effective management
Individual SNTs can be costly due to ongoing administrative costs and set-up and management fees. In contrast, PSNTs are affordable options offering lower thresholds for funding trusts, further reducing the burden on beneficiaries and their families.

Professional oversight
Nonprofit organizations managing PSNTs typically employ financial experts who oversee the investment and administration of funds. This professional management ensures the trust grows optimally, securing the beneficiary's financial future.

Maintaining government benefits
One of the primary advantages of any special needs trust is its ability to provide for the beneficiary without affecting their eligibility for government assistance programs. PSNTs are specifically structured to comply with these regulations.

Flexibility in contributions
You can contribute both first-party and third-party funds to PSNTs. This flexibility allows families to pool resources from various sources, including personal injury settlements, inheritances, and gifts.

Still, PSNTs are not without challenges. It's essential for families to carefully select the managing nonprofit organization, as the quality of management can significantly affect the trust's effectiveness. You should research the organization's track record, fee structure and the support services it offers.

Additionally, while PSNTs provide financial security, they also require diligent planning and ongoing oversight. Families should stay informed about changes in regulations that could affect the trust and regularly review its performance.

Translating SNTs and PSNTs Into Real Life (and Death)

Within the intricate framework of SNTs and PSNTs lie compelling personal stories. Many shed light on the pivotal role these trusts play in securing the well-being of those they serve.

Martin's story

Martin was a loving grandfather whose inadvertent misstep threatened the stability of his 20-year-old grandson, John's, financial future. Martin's failure to anticipate the implications of naming John as the direct beneficiary of a portion of his 401(k) left John at risk of losing his much-needed Medicaid and SSI benefits after Martin died.

However, Martin's son, Matthew, stepped in to rectify the situation, spearheading the establishment of a self-settled SNT funded by the inheritance from Martin's 401(k). While this trust was subject to the Medicaid payback provisions, it served as a lifeline for John, ensuring the restoration of his government benefits.

John's story shows how SNTs are not merely financial instruments but guardians of dignity and security for people with special needs.

Roger's story

Roger's journey underscores the multifaceted nature of self-settled SNTs, especially in healthcare planning. Roger, age 45, was a victim of medical malpractice. As a result, he found himself grappling with a myriad of health-related expenses alongside his existing disabilities. A qualified special needs planning attorney helped Roger through the complexities of Medicare liens and settlements. As a result, Roger was able to establish a Medicare set-aside arrangement within his SNT.

This strategic maneuver addressed Roger's ongoing healthcare needs and secured his eligibility for Medicaid and SSI. Roger's story is a testament to the transformative power of SNTs, offering individuals like him a pathway to financial stability amid adversity.

Jane's story

Jane's narrative took on a familial hue, showcasing the impact of parental foresight and unconditional love. Jane, also 45, battled schizophrenia from childhood. She relied on SSI and Medicaid for her living expenses. But her future became shrouded in uncertainty after her mother, Mary, died.

Mary's meticulous planning, however, included a third-party trust designed to protect Jane's interests long after her death. Mary's will passed on her house and assets to an SNT and the successor trustee, instead of directly to Jane. That allowed Jane to live in the house and use the assets to pay for other expenses, securing her financial stability without compromising her eligibility for vital benefits.

Maria's story

Maria is a single mother of a child with autism. She faces numerous challenges in ensuring her son's future is secure both financially and through planning. Through a PSNT managed by a reputable nonprofit organization, Maria was able to receive guidance and talk through legal and financial needs to help in the support of her son.

During enrollment with the nonprofit, Maria was able to fund a First Party PSNT with proceeds from a small inheritance her parents left directly to her son. In addition, the nonprofit was able to work with Maria to ensure the governmental benefits her son receives would be protected. The trust's professional management not only has preserved her son's eligibility for Medicaid and SSI but by establishing the PSNT has provided the opportunity to pay for those items not covered by his benefits to enhance his quality of life.

For more information, please contact your advisor.

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About the Author

As a Relationship Manager for Key Private Bank, Gretchen Miller focuses on ensuring her clients' wealth management plans are carried through to meet their unique financial objectives and grow and preserve wealth. Gretchen coordinates the implementation of wealth management strategies with the relationship team and ensures clients have the tools and information to keep track of their financial situations and make informed decisions. She also coordinates regular communications and updates with the team and delivers the latest insights and advice to benefit clients' particular situations.

Gretchen has more than 30 years of experience in financial services and is well-qualified to help clients implement strategies to achieve their goals. Most recently, prior to joining Key, Gretchen served as Director of Advanced Planning for Prudential Financial, where she was a subject matter expert on financial and estate planning and on retirement topics such as Social Security, Medicare, and tax-efficient distribution strategies. Gretchen earned a Bachelor of Science degree in Management from Springfield College and an MBA from the University of Phoenix. Gretchen obtained her certification as a Certified Financial Planner.™ Most recently, she obtained her Certified Divorce Financial Analyst® certification in 2023. She is a member of the Financial Planning Association, the Investments & Wealth Institute, and the Institute for Divorce Financial Analysts®.

About the Author

Cindy serves as the National Director of Philanthropic Advice at KeyBank, where she is responsible for introducing a comprehensive suite of sophisticated planning solutions tailored for nonprofit and institutional clients. Her role encompasses developing and implementing growth strategies, providing strategic planning advice, conducting governance and policy reviews, offering thought leadership, and delivering education on a range of critical topics. These topics include planned giving, fund accounting, charitable trusts, donor-advised funds, and other services that support nonprofits with a particular focus on Endowments, Foundations, and Pooled Special Needs Trusts.

Understanding the importance of supporting clients in the impactful work they do, Cindy obtained her Chartered Special Needs Consultant (ChSNC®) designation. This designation enables her to assist people with special needs through planning ideas. She has gained in-depth knowledge of the best strategies and a dynamic understanding of areas such as disability regulations, special needs trusts, the ABLE Act, government benefits, Medicaid complexities, special education, estate and retirement planning, and tax implications.

The Key Wealth Institute is a team of highly experienced professionals representing various disciplines within wealth management who are dedicated to delivering timely insights and practical advice. From strategies designed to better manage your wealth, to guidance to help you better understand the world impacting your wealth, Key Wealth Institute provides proactive insights needed to navigate your financial journey.

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