



SNT Beneficiaries on the Move: Third in a Series

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This series reviews the myriad issues that arise as a result of the increased mobility of the beneficiaries of Special Needs Trusts (SNTs). Special needs planning attorneys, and the other allied professionals with whom they collaborate (as described in the first article of this series), are increasingly called upon to help facilitate the transition of beneficiaries, and the SNTs they bring with them, from one jurisdiction to another. The second article of this series began a discussion of the “network” of third-party SNTs (TPSNTs) that [comprise a comprehensive special needs estate plan](#). This article continues that discussion.

The “Network” of Special Needs Trusts

Inter-Vivos Irrevocable Life Insurance TPSNT

In light of the current historically high federal estate tax exemption under the recently enacted Tax Cuts and Jobs Act (estimated at approximately \$11.2 million in 2018), fewer families are utilizing Irrevocable Life Insurance Trusts (ILITs) to own large life insurance policies that will be excluded from their gross estates for estate tax purposes. However, because the cost of fully funding the needs of a beneficiary with a disability (who may never be fully self-supporting) can be astronomical, one or more ILITs designed to hold very large life insurance policies may be included in the network of TPSNTs. This author prefers to design an ILIT as the owner and beneficiary of single-life or second-to-die policies insuring (typically) the beneficiary’s parent(s), with TPSNT provisions embedded within the trust agreement that establishes the ILIT.

Many families wish for the child with the disability to be the sole beneficiary of the TPSNT during the child’s life, while some are comfortable allowing their children without disabilities to be secondary permissible beneficiaries while the child with the disability is still living. Families are often concerned about “over-funding” the anticipated needs of the child with the disability. One option to address this concern is to divide the policy proceeds

paid to the ILIT into separate trust shares among the client's children and grandchildren, but provide that the child with special needs is also a secondary permissible beneficiary of his siblings' shares if the proceeds allocated to his own separate share prove insufficient to fully cover his needs.

As with the inter vivos gifting TPSNT discussed in the second article of this series, contributions to an ILIT that enable the Trustee pay the premiums on life insurance policies owned by the ILIT must be covered by powers of withdrawal held by the beneficiaries of the ILIT (other than the beneficiary with a disability) in order to qualify as "present interest" gifts that are eligible for the gift tax annual exclusion under IRC § 2503(b)(1). It is a frequent planning faux pas to grant the beneficiary of a TPSNT a power of withdrawal, which could disqualify him from ongoing eligibility for means-tested government benefits.

Inter-Vivos TPSNTs in the Context of Divorced Parents

The toll that a child's disability exacts on a marriage is often insurmountable. Many parents who have a child with a disability do end up in divorce court. After the divorce, the maternal and paternal grandparents of their grandchild with a disability often still wish to help secure their grandchild's future, but each "side" of the family wishes to designate different remainder beneficiaries of a TPSNT upon the death of the grandchild. This often necessitates two (or more) separate TPSNTs, contributions to which may have vastly different beneficiaries both during the life, and after the death, of the beneficiary with the disability.

If the divorce is amicable, it may be realistic to create a TPSNT to which each ex-spouse may freely and gratuitously contribute funds to secure the future of their child with a disability. However, [if the divorce settlement agreement](#), or a court order, mandates either ex-spouse to contribute to a SNT for their child with a disability (e.g. [in the form of child support](#)), then a TPSNT may not be used; rather, a first-party SNT would be required.

Inter-Vivos Community Fundraising TPSNT

Occasionally, the circumstances of a person's disability are so heart-wrenching that the greater community-at-large wishes to help secure that person's financial future with organized fundraising efforts. While paying donated funds directly to the parents or other relatives of the person with a disability may seem like an easy and uncomplicated approach, this often results in further heartache for both the well-intentioned community donors and the person with the disability.

The same reasons that obviate against disinheritance of a person with a disability and leaving that person's share of an estate to another person to manage informally also make this an imprudent approach in the context of a community raising funds for a person with a

disability. Even well-intentioned parties may fail to manage designated funds for the benefit of the person with a disability, for myriad reasons. If the person who is managing the donated funds informally commingles the assets with his own, and thereafter (i) files for bankruptcy, (ii) becomes party to a divorce proceeding and a subsequent equitable division of property, (iii) has a judgment lien recorded against him by a creditor, (iv) fails to pay his tax liabilities and becomes subject to a tax lien, or (v) dies intestate with heirs-at-law that include persons other than the intended beneficiary, or dies testate but fails to make proper provision in his Will for the ongoing management of the funds for the intended beneficiary, the intention of the community that raised the funds for the person with the disability will likely be defeated.

A carefully drafted TPSNT may serve as the repository for funds raised by well-intentioned donors in the community. To address the often problematic issue of an appropriate remainder beneficiary upon the death of the beneficiary with the disability, the trust agreement may designate a disability-specific charity or non-profit organization that focuses on the beneficiary's disabling condition, or that has supported the beneficiary's family in other ways.

Contributions to this type of TPSNT would not qualify as a "present interest" for purposes of the annual gift tax exclusion under IRC § 2503(b)(1) unless it is drafted to include appropriate powers of withdrawal. Most of these TPSNTs do not include the requisite withdrawal rights, thus requiring a donor to use a portion of his lifetime gift tax exclusion under IRC § 2010(c) when making a contribution. Furthermore, contributions to this type of TPSNT do not qualify for the charitable income tax deduction under IRC § 170(c), often to the surprise of the donors.

Inter-Vivos TPSNT to Serve as Designated Beneficiary of IRAs, 401(k)s, or other Qualified Plans

Almost every family will need a TPSNT designed as an "accumulation trust" to serve as the "designated beneficiary" of an IRA, 401(k) or other qualified plan account, which complies with complicated IRS regulations. See the excellent [Voice article](#) on this subject penned by SNA member Lisa Davis.

Inter-Vivos TPSNT to Serve as Income Beneficiary of Charitable Remainder Trusts

If a family is charitably inclined, it is possible to draft a TPSNT as a qualified income beneficiary of a charitable remainder trust (CRT) if it has a stated term not exceeding twenty years. At the end of the CRT term, the remainder could pass to a charitable organization which may have provided meaningful support to the beneficiary's family, or which is devoted to the specific disability by which the beneficiary is challenged.

A family's network of TPSNTs will vary depending on their circumstances and objectives. Consultation with an attorney and other advisors seasoned in handling the complex worlds of estate planning and disability planning is a prudent first step in designing an appropriate network of TPSNTs.

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