



## **Two Different Types of Special Needs Trusts**

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### **Third-Party Special Needs Trusts**

*Third-party SNTs are [commonly used by persons planning in advance for a loved one with special needs](#). Typically, the parents of an individual with disabilities or special needs will be the persons who establish a third-party SNT, although a grandparent, a sibling, or any other person (other than the beneficiary) may establish the SNT. Third-party SNTs can be included in a Last Will and Testament, established within an inter vivos trust that is designed to avoid probate (“Living Trust”), or drafted as a stand-alone SNT. These SNTs are typically funded upon the death of the beneficiary’s parents or the other individual(s) who established the SNT.*

*SNTs created under a Will or as a subtrust within a Living Trust do not come into existence (and therefore cannot receive gifts) until after the death of the individual whose Will or Living Trust created the SNT. Therefore, a stand-alone SNT may be more useful if there are multiple donors who wish to fund the SNT. A stand-alone SNT exists during the lifetime of the person establishing the SNT, which allows the SNT to receive gifts from grandparents, family friends or even the person establishing the SNT, prior to the death of the SNT’s creator. Such an SNT is available as a receptacle for lifetime and post mortem gifts from any third-party source.*

*This type of SNT does not have to be irrevocable in order to preserve the eligibility of the SNT beneficiary for means-tested public benefits. However, if the SNT beneficiary has the power to revoke the SNT, the SNT assets would be considered an available resource for Supplemental Security Income (SSI) and Medicaid purposes. The beneficiary's ability to revoke the SNT or otherwise exercise control over the SNT may render the beneficiary ineligible to receive public benefits that have an income or asset limit. The SNT agreement should authorize the person establishing the third-party SNT and/or the trustee to amend the SNT to address later changes in the law or the circumstances of the beneficiary. Allowing for such limited amendments helps ensure that essential government benefits are preserved if an agency challenges the terms of the SNT.*

*The most important difference between third-party SNTs and first-party SNTs (described below) is what happens to SNT property when the beneficiary dies. Upon the beneficiary's death, the third-party SNT is not required to use the remaining assets to reimburse any state(s) for the Medicaid benefits received by the beneficiary during his or her lifetime. As a result, this type of SNT is a useful planning tool for people who want to set aside property for a beneficiary with disabilities, preserve essential public benefits during that beneficiary's lifetime, and remain in full control of where all of the remaining SNT assets will go upon the beneficiary's death.*

### **First-Party Special Needs Trusts**

*First-party SNTs are most often used when the person with a disability inherits money or property outright, or receives a court settlement. These SNTs also are useful when a person without a prior disability owns assets in his or her name, later becomes disabled, and thereafter needs to qualify for public benefits that have an income or asset limitation. These SNTs are creatures of federal law, specifically (i) individual first-party SNTs are authorized under 42 U.S.C. § 1396p(d)(4)(A), and (ii) pooled first-party SNTs are authorized under 42 U.S.C. § 1396p(d)(4)(C). First-party SNTs also are commonly called self-settled SNTs, Medicaid payback trusts, OBRA '93 trusts, and d4A or d4C trusts.*

*Until the Special Needs Trust Fairness Act became law late in 2016, the only persons or entities authorized to "establish" (create) an individual first-party SNT were the SNT beneficiary's parent, grandparent, legal guardian, or a court. Since December 13, 2016, federal law also authorizes a mentally and legally competent SNT beneficiary to establish an individual first-party SNT. A first-party SNT is funded with property that belongs to the beneficiary, or to which the beneficiary is or becomes legally entitled. Property in a first-party SNT can only be used for the "sole benefit" of that beneficiary. Individual first-party SNTs may be created (and funded) only for individuals who meet the government's*

*definition of “disabled” and are under sixty-five years of age when the SNT is established (and funded).*

*While a pooled first-party SNT (described below) can be established by individuals over sixty-five years of age in many states, a significant number of states do not allow a person over age sixty-five to establish or transfer property to a pooled first-party SNT without penalty. Pooled first-party SNTs can be established by the beneficiary, the beneficiary’s parent, grandparent, or guardian, or a court. If the SNT beneficiary is not mentally and legally competent, then court approval must be obtained to fund the SNT with the beneficiary’s property.*

*All first-party SNTs must specify that after the beneficiary’s death, all amounts remaining in the SNT, up to an amount equal to the total lifetime medical assistance benefits paid on behalf of the beneficiary by the Medicaid program(s) of any state(s), are first repaid to those state Medicaid program(s), even to the extent of fully exhausting the remaining SNT assets. Only after this Medicaid payback may any balance be distributed to other remainder beneficiaries.*

*A legally competent person with a disability may have a first-party SNT established and funded without court involvement. However, annual accountings should be provided on an informal basis to the beneficiary and to the applicable Medicaid agencies. When a minor or mentally incompetent adult is legally entitled to receive funds from a lawsuit, an inheritance, or from any other source, then court approval to establish and fund the first-party SNT is required. Often, the court must make specific findings to ensure that the SNT is considered “exempt” when determining the beneficiary’s eligibility for public benefits that have income or asset qualification thresholds. These findings could include:*

- The minor or adult has a disability that substantially impairs the person’s ability to provide for his or her own care or custody, and constitutes a substantial handicap. In practice, a person who qualifies for SSI or Medicaid on the basis of disability is likely to satisfy the substantial impairment requirement.*
- The minor or adult is likely to have special needs and expenses that will not be met without setting aside assets in the SNT.*
- The property used to fund the SNT does not exceed the amount that appears reasonably necessary to meet the special needs of the minor or adult.*

### **Pooled Special Needs Trusts**

Pooled SNT programs can be used to establish both first-party and third-party SNTs. [Pooled SNTs are established and administered](#) by a non-profit association for the benefit of multiple beneficiaries. Pooled SNT programs have the following features:

- A separate account is maintained for each individual beneficiary of the pooled SNT, but the administrator pools the assets of all accounts for purposes of investment and management.
- A master trust agreement governs the separate accounts of all SNT beneficiaries pursuant to a “joinder” document.
- An account with the pooled SNT is established for the sole benefit of an individual with disabilities by the parent, grandparent, or legal guardian of the individual, by the individual personally, or by a court. The beneficiary of a first-party account must meet the government’s definition of “disabled.”
- While there is no express prohibition against establishing and funding a first-party account with a pooled SNT if the beneficiary is sixty-five years of age or older, most states do impose an eligibility penalty in that situation.
- For first-party accounts with pooled SNTs in all states any assets remaining in the beneficiary’s separate account upon his or her death, to the extent not retained by the pooled SNT, first must be used to reimburse the Medicaid program(s) of any state(s) that has provided medical assistance for the beneficiary. However, a state is not entitled to receive more than the amount remaining in the beneficiary’s separate account, even if the amount owed to the state is greater than the amount remaining in the deceased beneficiary’s separate account.

## **Conclusion**

Both first-party and third-party SNTs must be properly drafted in order to protect a beneficiary’s right to receive means-tested public benefits. The tax consequences of SNTs are not addressed in this article, but also are very complex. (Visit the index of prior issues of *The Voice* to discover those which specifically address various SNT tax issues.) To best protect the government benefits for which an individual with disabilities may be eligible, it is important to discuss which type of SNT should be used in a specific situation with an attorney who is proficient in special needs planning, including any of the Special Needs Alliance members found on the SNA website.

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