

Pooled and special needs trusts

First-Party Supplemental Needs Trust

A Special Needs Trust (SNT) can play an important role in preserving the financial security and lifestyle of a person with special needs. A properly drafted SNT allows the individual to benefit from supplemental resources while still qualifying for public benefits, such as Supplemental Security Income (SSI) and Medicaid. Generally, when a parent or guardian wishes to establish and fund a trust for the benefit of a minor child, the attorney recommends a “third-party” SNT be set up for the child. But, when the person with special needs has his or her own assets, another option may be more appropriate: the “first-party” or “self-settled” SNT.

What is a first-party SNT?

Like a third-party SNT, the first-party trust is designed to benefit individuals with special needs who qualify — or expect to one day require — public benefits that are available only to people with limited resources. Both third- and first-party SNTs allow assets to be set aside for “supplemental” expenses not covered by SSI or other resources. For example, a trustee can distribute SNT funds to pay for education expenses, a vacation, or hobbies, but not for food or shelter, which are covered by SSI.

What differentiates a first-party SNT is the following:

- The trust for a minor must be established by a parent, grandparent, guardian, or the court.
- The trust must be irrevocable.
- The beneficiary’s assets must be used to fund the trust.
- The beneficiary must be under age 65 at the time the trust is established.
- At the beneficiary’s death, the state Medicaid agency must be reimbursed.

When is a first-party SNT appropriate?

A first-party SNT may be desirable when an individual with special needs has assets — or expects to receive assets — that would disqualify him or her from eligibility for public benefits. Some examples include:

- An inheritance. Receiving an inheritance can cause a person with special needs to lose public benefits. That outcome may be prevented by placing the inherited assets in a first-party SNT.
- A settlement from a lawsuit. A first-party SNT can allow an individual to receive an award in a personal injury or medical malpractice case without losing eligibility for public benefits. Settlements often comprise a lump-sum payment and an annuity. Both types of payment can be directed to a first-party SNT established by the court.
- A divorce settlement. If a spouse with special needs is unable to work and qualifies for public benefits, it may be helpful to have a first-party trust incorporated into the divorce settlement. For example, when the settlement calls for the working spouse to pay the non-working spouse both a lump-sum equitable distribution and monthly alimony, both types of payment can be directed to the trust, rather than to the spouse. The spouse with special needs can then obtain monthly income through SSI and have medical expenses covered by Medicaid.

Third-Party Supplemental Needs Trust

Special needs trusts come in three main forms — first-party special needs trusts, third-party special needs trusts, and pooled trusts. All three trust varieties are designed to manage resources for a person with special needs so that the beneficiary can still qualify for public benefits like Supplemental Security Income (SSI) and Medicaid. While first-party special needs trusts and pooled trusts hold funds that belong to the person with special needs, third-party special needs trusts, as the name implies, are funded with assets that never belonged to the trust beneficiary, and they provide several advantages over the other two types of trusts.

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Third-party special needs trusts are set up by a donor – the person who contributes the funds to the trust. These trusts are typically designed as part of the donor’s estate plan to receive gifts that can help a family member with special needs while the donor is still living and to manage an inheritance for the person with special needs when the donor dies. Third-party special needs trusts can be the beneficiaries of life insurance policies, can own real estate or investments, and can even receive benefits from retirement accounts (although this process is very complicated and not typically recommended unless there aren’t other assets available to fund the beneficiary’s inheritance). There is no limit to the size of the trust fund and the funds can be used for almost anything a beneficiary needs to supplement her government benefits. Upon the beneficiary’s death, the assets in a third-party special needs trust can pass to the donor’s other relatives or anywhere else.

This last factor is one of the key advantages of a third-party special needs trust: because the funds in the trust never belonged to the beneficiary, the government is not entitled to reimbursement for Medicaid payments made on behalf of the beneficiary upon her death, unlike with a first-party or pooled trust. This allows a careful donor to benefit her family member with special needs while potentially saving funds for other people who don’t have the same needs.

Whereas first-party trusts must be established for the benefit of someone who is younger than 65, third-party trusts don’t have age limits. In some states, first-party trusts must be monitored by a court, but third-party trusts almost never have to go through this same process, especially while the donor is still alive. In addition, while the donor is living, funds in the trust usually generate income tax for the donor, not for the beneficiary, avoiding the complication of having to file income tax returns for an otherwise non-taxable beneficiary and then explain them to the Social Security Administration.

Although a third-party special needs trust has many advantages, it is not always a viable option for families of people with special needs. One of the major drawbacks of a third-party trust is its absolute inability to hold funds



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belonging to the person with special needs. So if the trust beneficiary receives an inheritance that wasn’t directed into the special needs trust to begin with or if she settles a personal injury case, the funds have to be placed in either a first-party trust or a pooled trust, since even one dollar of a beneficiary’s own money could taint an entire third-party trust. But even with these restrictions, most people trying to help a family member with special needs are going to at least need to strongly consider drafting a third-party special needs trust.

Pooled Trusts

Because beneficiaries of programs like Supplemental Security Income (SSI) and Medicaid must be quite poor to qualify, they can lose their benefits when they come into an inheritance, receive money in their own names from an accident settlement, or merely accumulate too much money in a bank account. Beneficiaries can prevent this from happening by transferring their excess assets into an individual or first-party special needs trust, also known as a (d)(4)(A) trust. However, these trusts can be costly to set up. A “pooled trust” presents another option.

A pooled trust, also known as a (d)(4)(C) trust, is a special needs trust with a twist. While an individual special needs trust is created for one’s self or by someone for the benefit of a specific beneficiary who is often a family member, a pooled trust is established by a nonprofit organization, with individual beneficiaries creating accounts within the larger trust. In other words, the assets of many people with special needs are “pooled.” Because a pooled trust accepts contributions from many beneficiaries, the trust is able to make more

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stable investments and provide additional management services that a plain vanilla special needs trust might not be able to afford. On top of these benefits, transfers into a pooled trust, like transfers into a first-party special needs trust, do not prevent a person with special needs from accessing government benefits.

Although the funds placed in a pooled trust are invested together, each beneficiary's account remains his own. Depending on the trust, a beneficiary might work with a social worker or other trust advisor to tailor a funds distribution plan that fits his lifestyle. As with an individual special needs trust, funds in a pooled trust are used to supplement a beneficiary's government benefits, and the funds can be used to pay for reoccurring bills, clothes, and other expenses. Importantly, beneficiaries looking to spend down their assets in order to qualify for, or remain on, government benefits can transfer funds directly into a pooled trust account without having to rely on a family member's help.

Like most trusts that allow people with special needs to qualify for benefits, pooled trusts come with a catch. As with an individual (d)(4)(A) trust, upon a beneficiary's death, most states require that the funds held in a pooled trust account must be used to reimburse the government for any medical services provided while the beneficiary was alive. However, the state often allows the nonprofit organization that established the pooled trust to retain a percentage of a deceased beneficiary's account to support its mission.



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When should a person with special needs consider a pooled trust?

While each beneficiary's situation is different, a person who has only a small amount of money in her name may like the low cost of a pooled trust. Others appreciate the fact that their funds will be used to help others with special needs.

For more information about Special Needs Trusts or nonprofit donations, [please contact National Director of Philanthropic Advice, Cynthia J. McDonald at 518-257-8745.](#)



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