

ABLE Act Considerations for Estate Planning

by Philip Herzberg, CFP®, CTFA, AEP®



Philip Herzberg, CFP®, CTFA, AEP®, is a client adviser for The Lubitz Financial Group in Miami, Florida. He is president of FPA of Florida, past president of FPA of Miami, and a

member of the Estate Planning Council of Greater Miami Board of Directors.

ON DECEMBER 19, 2014, President Obama signed into law the Achieving a Better Life Experience Act. This Act added a section, Section 529A, to the Internal Revenue Code (IRC) to allow for the creation of a new type of qualified, tax-advantaged savings account, termed an ABLE account (or 529A account).

As planners, how do we incorporate the ABLE account into our estate planning to provide a better quality of life for those with special needs? Be cognizant that individuals with disabilities face significant challenges in finding and sustaining employment, as well as living independently, because their access to safety net programs, such as Supplemental Security Income (SSI) and Medicaid can be lost once they establish resources of \$2,000.¹

ABLE Act Basics

First, understand that an eligible individual—referred to as the designated beneficiary and owner of the account—fulfills the requirements if, during the taxable year, the individual is entitled to Social Security benefits based on a

blindness or disability that occurred before the date on which the individual turned age 26. Your client need not be under the age of 26 to qualify to open an ABLE account. Further, your client could be over the age of 26, but must have the documentation of disability that indicates age of onset before the age of 26.

Know that contributions may be made to an ABLE account established for the purpose of meeting the qualified disability expenses of the account's designated beneficiary. The program must limit a designated beneficiary to one ABLE account.

Note that a qualified ABLE program is set up and maintained by the state in which the eligible individual resides, or another state if the state has a contract with the eligible individual's resident state. Akin to IRC Section 529 college savings, a qualified ABLE program is managed by a financial institution and administered and run by the state in which the eligible client resides. Alternatively, a qualified ABLE program can be maintained by another state if the state has a contract with the eligible client's resident state. Similar to the Section 529 higher education plan mechanism, the ABLE program limits investment changes by the account holder to two times per year.

Understand that the state must operate its program under federal guidelines, which specify that contributions to an ABLE account are treated as completed gifts of present interest, eligible for the gift tax annual exclu-

sion. There is a \$14,000 annual limit on non-deductible cash contributions from all account contributors. Excess contributions above this current annual gift exclusion amount are subject to adjustment for inflation in future years and to an excise tax.

Qualified ABLE account assets are not subject to the current income tax and thus accumulate on a tax-free basis. Even though contributions to an ABLE account are not tax deductible for federal income tax purposes, they may be deductible for state income tax purposes.

Rollovers are an additional ABLE account benefit, as amounts in one ABLE account may be rolled over tax-free to another ABLE account for the same beneficiary. Be aware that no more than one such rollover may be made within a continuous 12-month period. Moreover, the funds must be deposited into the new ABLE account within 60 days of being distributed from the prior account.

Planning Insights for Using ABLE Accounts

What do you need to know about the effect of ABLE accounts on federal means-tested programs? In essence, the ABLE accounts are likely to be most appealing for those with disabilities who work and seek to save more than \$2,000, as well as for the families who need a place to deposit gifts or inheritances from family members.

Be cognizant that any distribution from an ABLE account for qualified disability expenses is generally disregarded

Journal of Financial Planning

Submission Guidelines

The long-standing tradition of the *Journal of Financial Planning* is to provide groundbreaking research for practitioner use in real-life planning with clients, and to champion the effort to align scholarly research and practitioner needs that foster the greatest collaboration of talents in the field.

There is no better venue through which to influence the way financial planning is practiced and financial planning clients are served than the *Journal of Financial Planning*.

You'll find writing and submission guidelines at FPAJournal.org.



Papers published in the *Journal* this year will be considered for the 2016 Montgomery-Warschauer Award.

for the purposes of determining eligibility for federal means-tested programs such as SSI or Medicaid. Understand that the individual's SSI benefits will be suspended once the account balance surpasses \$100,000, but eligibility for Medicaid is unaffected. Spending ABLE account money on housing may reduce SSI payments, too.

What if distributions are made for expenses not related to the beneficiary's disability or blindness? Inform your clients that these non-qualified withdrawals distributed in excess of qualified disability expenses are subject to tax amounts calculated under IRC Section 72 rules, plus a 10 percent penalty.

ABLE accounts are not sensible for families who wish to fund larger dollar amounts on behalf of a disabled beneficiary over time in excess of the maximum account limit. Note that any amounts remaining in the deceased beneficiary's ABLE accounts are subject to a claim from the state for an amount equal to Medicaid paid for by the state, after all outstanding qualified disability expenses have been paid.

ABLE Accounts versus Special Needs Trusts

Conversely, special needs trusts, which are created and funded by a third party, are generally not subject to this Medicaid payback provision. After assets are used for the supplemental needs of the beneficiary, any remaining assets can fully flow to the surviving family members or other beneficiaries after death of the disabled beneficiary without any requirement to repay the state for aid given.²

Realize that the special needs trust can be established for any age beneficiary during life or at the grantor's death. Moreover, there are no dollar limits on the amounts that can be contributed to or accumulated in the trust. If the special needs trust meets the "qualified disability trust" require-

ments, up to \$14,300 (in 2015) of taxable income may avert tax.³

The caveat is that rules governing these special needs trusts are complicated and differ by state and by the source of the funds. Educate third-party fund trustees to be prudent when making distributions as they need to avoid paying money directly to the disabled beneficiary in order to preserve eligibility for government programs. Ascertain that parents, relatives, and trusted allied professionals coordinate beneficiary designations on retirement accounts and life insurance policies so that gifts or inheritances should also pass to the special needs trust.

How can an ABLE account be used in conjunction with a special needs trust to enhance a family's ability to provide for a disabled child's care? Be mindful that an ABLE account can allow for more choice for the beneficiary and family. The owners of an ABLE account will have the flexibility to control their funds, and if circumstances change, still have the special needs trust available to them.

Assessing which option is more appropriate will depend upon the individual's situation. For families saving for a disabled child's future, the ABLE account will serve as a significant and viable supplement to the special needs trust. ■

Endnotes

1. See "Incorporating the ABLE Act into Special Needs Planning" by John Nadworny in the May 2015 issue of the *Journal of Financial Planning*.
2. See "Will Section 529A ABLE Accounts Replace the Need for Disabled Beneficiary Special Needs Trust?" by Michael Kitces, posted March 4, 2015 on Kitces.com.
3. See "ABLE Accounts: An Option for Families with Disabled Children" by Randy Gardner and Leslie Daff in the February 2015 issue of the *Journal of Financial Planning*.