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INTRODUCTION

This article focuses on problems faced by parents[1] who wish to make lifetime[2] gifts to a disabled child.[3] Although lifetime giving

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1. This article focuses on parent(s) and a disabled child or children. Of course, the proposals made are equally applicable to grandparents, or other relatives, or friends who may be motivated to make gifts.

2. Most of the literature in this area deals primarily with testamentary giving, *See, e.g.*, McMullen, *Family Support of the Disabled: A Legislative Proposal to Create Incentives to Support Disabled Family Members*, 23 U. MICH. J. L. REF. 439, 439 (1990); Frolik, *Estate Planning for Parents of Mentally Disabled Children*, 40 U. PITT. L. REV. 305, 316 (1979)[hereinafter Frolik, *Estate Planning*]. However considering the effect of compounding of interest, the advantages to be gained from the use of the federal gift tax annual exclusion for gifts, I.R.C. § 2503 (1991), and the opportunity of using monies for a disabled child's development at a relatively early age, lifetime giving actually presents the most effective planning tool for middle and upper class parents.

3. Who is to be considered "disabled" for purposes of liberalizing lifetime giving is a difficult issue. There is no generally accepted definition of "disability." Note, *The Rehabilitation Act of 1973*, 30 WM. & MARY L. REV. 149, 150 (Fall 1988). It is not always clear whether or not a person will be legally "disabled" until the child has met a certain level of maturity.

To simplify the discussion in this article, the standard of disability used for purposes of Supplemental Security Income (SSI) is applied. According to the rules for SSI, a child is regarded as disabled if she suffers from "any medically determinable physical or mental impairment of comparable severity" to an impairment that would render an adult disabled under the Act. 42 U.S.C. § 1382c(a)(3)(A) (1990). Under the Social Security Act an adult is disabled if he is "unable to do his previous work" and unable to engage in "any other kind of substantial work which exists in the national economy" as a result of his impairment, 42 U.S.C. § 1382c(a)(3)(B) (1990).

If the suggestions made in this article are to be put into effect, it might be appropriate to require parents to file a form with the Internal Revenue Service to claim "disability." Such a filing could then be subject to audit. Another possibility would be to allow a physician to certify a disability based on published guidelines. The use of the guidelines used for special should be encouraged both for the benefit of the disabled child and society,[4] at present, our government entitlement programs actually discourage parents from lifetime giving.[5] Thus, special Supplemental Security Income as well as Medicaid eligibility rules should be enacted to effect the expansion and facilitation of lifetime giving to the disabled. In addition, Congress should enact a special federal gift tax rule for lifetime gift giving.[6] The goal of these changes is to encourage a parent of a disabled child to invest in that child's future in the same way that a parent invests in the future of a non-disabled child.

THE PARENTS' DILEMNA

While parents are not generally obligated to support their children past the age of majority,[7] many parents have a natural desire to do so, especially in the case of a disabled child.[8] For parents of a disabled child, providing continuous security, comfort and care for their child after the parent's death is often an utmost concern.[9] Unfortunately, parents[10] soon realize that they face formidable obstacles if they attempt to provide security for their disabled child, because government entitlement programs are only available to individuals without adequate income.[11] Consequently, any gift by a parent to a disabled individual has the potential to render that individual ineligible for governmental assistance.

Public support programs such as Supplemental Security Income

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education would also be possible.

4. *See generally* Davis, *Financial & Estate Planning for Parents of a Child with Handicaps*, 5 W. NEW ENG. L. REV. 495, 507 (1983).

5. *See infra* text accompanying note 11.

6. *See infra* text accompanying note 38. This suggestion is not original. *See* McMullen, *supra* note 2; Whitman, *Present Policies Do Not Benefit Disabled Children* (Guest Editorial), TR. & EST., Apr. 1989, at 10.

7. *See, e.g.*, CONN. GEN. STAT. § 46b-215 (1987); ILL. REV. STAT. ch. 23, para. 10-2 (1988).

8. Leimberg & Hinkle, *Financial and Estate Planning for Parents of the Disabled*, J. AM. SOC'Y CLU & CHFC, May 1989, at 38-39.

9. A. Kadushin, CHILD WELFARE SERVICES 9 (3d ed. 1981).

10. *See* Frolik, *Estate Planning*, *supra* note 2, at 321-22.

11. Examples of federal programs are SSI and Medicaid. *See infra* text accompanying notes 12-17. State programs tend to either supplement or administer the federal programs. For example, CONN. GEN. STAT. § 17-108 (1988) provides funds for disabled persons to supplement what they would receive from SSI; § 17-134a allows the state to administer medical assistance funds granted to the state under Title XIX of the Social Security Act.

The eligibility requirements for federal assistance programs is discussed at *infra* text accompanying notes 15-17.

[hereinafter SSI][12] and Medical Assistance [hereinafter Medicaid][13] condition the availability of benefits on strict financial eligibility standards.[14] Once it is established that an individual is disabled, SSI and Medicaid have a two-pronged financial eligibility test.[15] An applicant can neither have "available resources" nor "income beyond prescribed amounts" and still qualify to receive established benefit levels.[16] The SSI/Medicaid definition of income is very broad and specifically includes gifts to the applicant, whether in cash or in kind.[17]

Other government assistance programs, both on the state and national level,[18] such as residential placement of disabled individuals, are made available without regard to income and assets.[19] However, the costs of these programs are charged to the user in proportion to her income and assets.[20] Eligibility standards for state programs vary from state to state.[21]

All of these benefits are seen as so valuable to the disabled child that trust and estate lawyers routinely caution parents not to place any savings in their child's name, or in a trust to benefit the child.[22] If the child needs public assistance in the future, any private resources that the child may have will either render the child ineligible for such assistance or will be taken by the government, dollar for dollar, as payment for the services provided to the disabled.[23]

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12. 42 U.S.C. § 1381 (1990). Supplemental Security Income provides a guaranteed annual income by means of cash payments to the aged, blind, and disabled. *Id.*

13. 42 U.S.C. § 1396 (1990). Medicaid provides health insurance benefits, often to individuals who would be otherwise uninsurable. *Id.* For this reason, Medicaid is often considered the most valuable of the entitlements.

14. R. MYERS, SOCIAL SECURITY 413 (1975).

15. 20 C.F.R. § 416.1100 (1990).

16. 20 C.F.R. § 416.1102; § 416.1201(a) (1989).

17. 20 C.F.R. § 416.1102 (1990). "Available resources" under § 416.1201(a) include cash, other liquid assets or property, real or personal, that could be converted to cash to be used for support and maintenance. Under 42 U.S.C. § 1382(a)(3)(A) & (b), the prescribed limits for countable resources are $2,000 for an individual and $3,000 for a couple. Retention of assets over this very minimal amount in a disabled person's name, with certain exceptions (*e.g.*, an owner-occupied home), can cause a dollar for dollar reduction in the amount of SSI benefits or can cause ineligibility for benefits altogether. 20 C.F.R § 416.1212.

18. Frolik, *Discretionary Trusts for a Disabled Beneficiary: A Solution or a Trap for the Unwary?*, 46 U. PITT. L. REV. 335, 338 (1985).

19. *Id.* at 335.

20. *Id.*

21. *Id.* at 320; *see* CAL. GEN. LAWS ANN., act 611 (Deering 1991); 1991 Ill. Laws 447.

22. Davis, *Financial and Estate Planning for Parents of a Child with Handicaps*, 5 W. NEW ENG. L. REV. 495, 507 (1983).

23. For regulations regarding limits on earned income, see 20 C.F.R. §§ 416.1104, -

When parents refrain from making lifetime gifts to their disabled children, it protects the child's eligibility for government benefits, but is an unsatisfactory result for the child, the parent and society-at-large. It lessens the child's chance to become a productive and independent citizen, and condemns her to a life of dependence on potentially inadequate government benefits. Reciprocally, it places an extremely heavy burden on the government and society, who are forced to support the child for her entire lifetime.

In certain cases, lawyers may also counsel parents to create a discretionary trust.[24] However, the discretionary trust also has drawbacks.[25] First, to be effective the trust must sharply limit the trustee's discretion to benefit the disabled child.[26] In addition, there is doubt about whether such an arrangement will be able to shield this trust from the federal eligibility requirements effectively, due to the vagaries of government tax policy. A discretionary trust that appears effective by today's standards may prove to be vulnerable to reimbursement to the government in later years.[27] Given that such a trust

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.1110 to -.1112 (1990); for regulations regarding limits on unearned income, see 20 C.F.R. §§ 416.1120 to -.1124 (1990).

24. A trust is considered a discretionary trust if by the terms of the trust it is provided that the trustee pays to the beneficiary only so much of the income and principal as the trustee in his uncontrolled discretion shall see fit to pay. RESTATEMENT (SECOND) OF TRUSTS § 155 (1957). The beneficiary cannot compel the trustee to pay any part of the income or principal. *Id.*

A discretionary trust can shelter funds intended for a disabled child from the reach of the governmental agencies which provide services to the child and insure that the child remains qualified for government assistance programs. Mooney, *Discretionary Trusts: An Estate Plan to Supplement Public Assistance for Disabled Persons*, 25 ARIZ. L. REV. 939 (1983). However, to accomplish this result the trust must be limited in the following manner: the disbursement of the principal and income of the trust must be wholly within the discretion of the trustee without any obligation to provide for the welfare or support of the child. *Id.* Otherwise, the beneficiary will be considered to have a property right in the trust and the trust will be included when determining eligibility for government benefits. *Id.* It will also be subject to reimbursement claims by the government. *Id* .

Connecticut has created a non-profit public corporation called Planned Lifetime Assistance (PLAN), whose purpose is to establish self-sufficiency trusts for the disabled. 65 CONN. B.J. 56 n.15. (1991). Trust participants pool assets in a private trust for investment. *Id.* The assets are then distributed according to the life care plan devised by family and program counselors. *Id.* This program does not permit the broad use of funds for a disabled person. *Id.* Rather, it fills the limited need to allow families to provide nonessential extras for a disabled child without running afoul of the eligibility requirements of public assistance programs. *Id.* For a disabled child who might, with adequate help, become self-sufficient, this type of limited trust might actually prove to be counterproductive. *Id.*

25. *Id.*

26. Frolik, *Estate Planning*, *supra* note 2, at 327.

27. In the area of tax reform, recent history shows that the government is not loath to change the rules abruptly, thereby invalidating past practices which were designed to take

must be irrevocable, a change in the law could, therefore, permanently disqualify the disabled from receiving federal subsidies.

In sum, therefore, parents often opt out of any attempt to provide for their disabled child, leaving the government with the full burden of supporting the child for her entire life. This can happen even where there are adequate funds for the parents to supplement their child's income, and where the parents would otherwise be eager to help.

A CHANGE IN THE SYSTEM IS REQUIRED

In order to improve this situation, the eligibility rules of SSI, Medicaid, and other benefits programs, should be changed to allow disabled children to qualify for government assistance and still be allowed to receive lifetime gifts.[28]

A. *Proposal for Special SSI and Medicaid Eligibility Rules*

Professor Judith McMullen has recently examined the problem of gift giving to disabled children and its effect on government assistance programs in her article entitled *Family Support of the Disabled: A Legislative Proposal to Create Incentives to Support Dis-*

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advantage of then existent tax policies. *See, e.g.*, Abramson, *Tax Law Put Restrictions on Individual Retirement Accounts*, Wash. Post, Nov. 15, 1987, at R24.

28. There is some indication that there may be, on the state level, a changing attitude towards government entitlement. In a recent article, Clifton B. Kruse, Jr. discusses three states, California, Texas and Missouri which allow parents and others to make lifetime gifts to disabled persons without those gifts being taken by the state for support and maintenance of the disabled person. Kruse, *Welfare Without Guilt: Benefiting from a Supplemental Needs Trust*, PROB. & PROP. 33 (May/June 1991).

California shields trusts established for disabled persons from reimbursement to government assistance programs. CAL. PROB. CODE § 15306(b) (Deering 1991). This law, however, does not act as a shield in a case where the trust would render the beneficiary ineligible for government assistance. *Id.*

Texas provides that, where the beneficiary is a mentally retarded person, a trust of $50,000 or less shall not be considered part of the beneficiary's property and shall not be liable for the support and maintenance of the person, regardless of age. TEX. REV. CIV. STAT. ANN. art. 5547-300 § 61(g) (Vernon 1991). The statute requires that the trust instrument be in writing, that a copy of the instrument be provided to the state and that the trustee will be required to provide a financial statement to the state upon request. *Id.*

The Missouri Family Trust Fund, which applies to Missouri domiciliaries who are mentally or physically impaired, requires that state agencies, unless prohibited to do so by federal law or regulations, disregard the existence of a trust fund when determining eligibility for public assistance, and that the existence of such funds cannot reduce, impair or diminish the benefits which the beneficiary might be entitled to under state law. MO. REV. STAT. § 402.200 (1990).

abled Family Members.[29] She illustrates that the current eligibility requirements discourage testamentary giving and suggests that Congress create limited exceptions to the eligibility requirements for a disabled child.

This suggestion could easily be modified to promote lifetime giving. Under such a plan, parents of disabled children would be able to establish a "qualified trust." Under a new exception to SSI eligibility requirements,[30] trust funds would be allowed to supplement SSI benefits and thus improve the quality of life for the designated disabled child. Under new rules, such an arrangement would create a "proportional, not dollar-for-dollar," reduction in SSI benefits for every payment from a trust to a disabled person.[31]

A "qualified trust" would thus create a monetary benefit to the beneficiary, as well as reducing the burden on public assistance programs.[32] There is a natural incentive for parents to establish the trust as early as possible to maximize interest accumulation. If the federal rules are changed to allow for a "qualified trust," a complementary modification in state laws will also be required.[33]

Because the trust could be employed to render tax-free otherwise legitimate taxable income, McMullen would require that the beneficiary receive all the trust income and that upon the beneficiary's death either a percentage of the trust be returned to the government or the remaining balance be taxed.[34] This provision, according to McMullen, would avoid manipulation of trust income to evade taxation.[35] McMullen analogizes these restrictions to the existing restrictions under the currently allowed Qualified Terminable Interest

29. McMullen, *supra* note 2. Professor McMullen focuses primarily on testamentary giving, but mentions that her idea could also be used to protect lifetime gifts to disabled children. *Id.* at 442 n.15.

30. McMullen uses the SSI regulations as an example but would similarly alter other eligibility provisions of public assistance programs. *Id.* at 458 n.95.

31. For every dollar of trust support received by a beneficiary, that beneficiary could lose 50 cents of SSI benefits. *Id.* at 459.

32. Under McMullen's plan "[t]here would be a limit to the amount of money which could be received from the trust while still receiving SSI benefits. . . ." For example, if SSI benefits were reduced fifty cents for each dollar received from the trust, the beneficiary could receive twice the dollar value of his SSI benefits from the trust before becoming ineligible for SSI. *Id.* at 459 n.96.

33. The extent of the changes required would depend upon the state rules. For example, some states' eligibility rules mirror those of the federal government; such a state would probably adopt changes which would mirror the federal changes. In other states, readjusting eligibility rules to comport with federal changes could involve a more complicated process.

34. McMullen, *supra* note 2, at 459.

35. *Id.*

Property (QTIP) Trust.[36] In establishing the QTIP provisions, and the marital deduction provisions in general, Congress adjudged that the surviving spouse, who may use the assets in the trust during her lifetime, should be subject to the federal estate tax at her death.[37]

B. *Gift Tax Proposal: Modification of I.R.C., Section 2503*

Finally, Congress should amend the federal gift tax rules to create a "disabled child" exception to the current requirement that the assets of a present interest gift be transferred to the child upon her attaining age twenty-one.[38] Currently, under I.R.C., section 2503(b), in order to obtain the $10,000 per donee annual exclusion from gift taxation the donor must make a gift of a "present interest."[39] Recognizing that parents may have legitimate concerns about giving property outright to a minor or giving the immediate right to income to a minor, Congress permits a gift to a minor to qualify for the present interest annual exclusion if three requirements are met.[40] First, the property and income from it must be available for the benefit of the minor until he reaches twenty-one.[41] Second, to the extent that the property and income are not spent for the minor's benefit, they must be payable to the minor when he reaches twenty-one.[42] Third, any unexpended property and income must be payable to the minor's estate or as the minor may appoint under a general power of appointment.[43]

Making a gift of a present interest under section 2503(c) is

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36. *Id*; *see* I.R.C. § 2503(b)(7) (1986).

37. *See* McMullen, *supra* note 2, at 461.

38. As an alternative to a revision of the gift tax, it would be possible to allow for the creation of an inter vivos trust with spend-thrift provisions. The trust would have to contain "Crummey" provisions, *Crummey v Commissioner*, 397 F.2d 82 (9th Cir. 1968), which would give the beneficiary the annual right for a reasonable period to demand the amount of any additional property transferred by gift to the trust, thereby making the gift to the trust qualify as a "present interest" as required by I.R.C. § 2503. *See infra* text accompanying note 39. The trust could be drafted so that it would continue over a much longer period of time than a trust for a non-disabled child. State statutes would have to protect the trust from being considered for purposes of eligibility for public assistance and to allow for a proportional, not dollar for dollar reduction in benefits when distribution occurs.

39. I.R.C. § 2503(b) (1986). A present interest is defined as an unrestricted right to the immediate use, possession, or enjoyment of property or the income from property. 26 C.F.R. § 25.2503-3(b).

40. I.R.C. § 2503(c) (1986).

41. I.R.C. § 2503(c)(1) (1986).

42. I.R.C. § 2503(c)(2)(A) (1986).

43. I.R.C. § 2503(c)(2)(B) (1986).

somewhat problematic for parents of a disabled child.[44] The requirement of 2503(c)(1) that the assets be turned over to the child at the age of twenty-one[45] is likely to be impracticable in a situation involving a disabled child; that child may never be capable of independently managing his or her own funds. In order to facilitate gift-giving to such a disabled child, the author proposes to add a new section, 2503 (d). It could read:

> (d) *Transfer for the Benefit of a Disabled Minor*-No part of a gift to an individual who is classified as disabled for purposes of receiving benefits under the Social Security Act[46] shall be considered a gift of a future interest in property for purposes of subsection (b) if the property and income therefrom-
>
> (1) may be expended by, or for the benefit of, the donee during his lifetime, and
>
> (2) will to the extent not expended be payable to the estate of the donee or as he may appoint under a general power of appointment as defined in section 2514(c).

SUMMARY

The parents of a disabled child bear heavy burdens, emotionally, physically and financially. The government entitlement and tax system, as it now stands, only adds to these burdens by acting as a strong disincentive for parents who wish to provide funds for the future of their disabled children.[47] If these parents make a lifetime gift to their disabled child, the likely result is a dollar by dollar reduction in public assistance to their child until their gift is expended.[48] Liberalizing the law to allow for qualified trusts for the disabled that would cause only a proportional reduction of benefits would be helpful to parents, the disabled and our society.

Changing the tax code to make it possible for parents to give funds to their disabled children at an early age would facilitate the building of a substantial fund over the course of the parents' life-

44. HECKT, *Reaction Comment*, THE MENTALLY RETARDED CITIZEN AND THE LAW 134 (1976).

45. *But see Commissioner v. Herr*, 303 F.2d 780 (3rd Cir. 1962) (extension of a trust beyond age 21 does not completely destroy "present interest exclusion").

46. For simplicity, the authors are using the SSI guidelines to define disability. There are, of course, other methods available to determine disability for these purposes. *See supra* note 3.

47. Whitman, *supra* note 6, at 10.

48. In effect, the parents would be making a gift to the government rather than the child for the child would receive no additional benefit. Frolik, *Estate Planning*, *supra* note 2, at 317.

times to provide for care for that child when the parents die. Congress has seen fit to enact special tax provisions for the benefit of special groups such as minors and widows.[49] Disabled children also deserve special attention.

49. *See, e.g.*, I.R.C. §§ 2503(c), 2523 (gift tax provisions for children and spouses), 2056 (estate tax marital deduction).