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TAXATION

Achieving a Better Life Experience (ABLE) Act of 2014

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The Achieving a Better Life Experience Act of 2014 (the “ABLE Act”) was signed into law by President Obama on December 19, 2014. The Act amends the Internal Revenue Code by inserting Section 529A, which provides for the tax treatment of ABLE accounts established for the care of individuals with disabilities. Other sections of the United States Code are also amended as necessary to effectuate the intent of the ABLE Act. The stated purposes of the ABLE Act are as follows:

(1) To encourage and assist individuals and families in saving private funds for the purpose of supporting individuals with disabilities to maintain health, independence, and quality of life.

(2) To provide secure funding for disability-related expenses on behalf of designated beneficiaries with disabilities that will supplement, but not supplant, benefits provided through private insurance, the Medicaid program..., the supplemental security income program..., the beneficiary’s employment, and other sources. (Section 101)

Both Medicaid and Supplemental Security Income (“SSI”) benefits are “need based”. In order to qualify, the value of an individual’s countable resources cannot exceed \$2,000. The ABLE Act allows a tax-free savings account to be established for the benefit of a qualified beneficiary without disqualifying the beneficiary for Medicaid regardless of the amount in the account. For purposes of SSI, the account may not exceed \$100,000. If the ABLE account balance exceeds \$100,000 at any time, the beneficiary’s SSI benefits will not be terminated but will be suspended until the account falls below \$100,000. In addition, the accounts cannot exceed the limitations imposed on qualified tuition plans, also known as 529 accounts, which limit plan contributions to the actuarial estimated cost of five years of undergraduate college. In New Jersey the cap on a 529 account is \$305,000.

Except in the case of a rollover from another ABLE account (which may be required if the beneficiary relocates to another state), the aggregate annual contributions to a beneficiary’s account from all contributors cannot exceed the annual gift tax exclusion amount (presently \$14,000). The contribution will be treated as a gift of a present interest to the beneficiary, which gift qualifies for the annual gift tax exclusion. Contributions must be in cash not property; therefore the gifts cannot be leveraged. The contributions are not deductible for federal income tax purposes, but the amounts in the account will accumulate on a tax-deferred basis. Although the income is not taxed while accumulating in the account, it will be taxed to the beneficiary when distributed but only to the extent distributed in excess of the qualified disability expenses. Thus the earnings will never be taxed if used for qualified disability expenses. The portion of the excess distribution includable in gross income will be calculated in a manner similar to that used

for taxation of an annuity. The portion of any distribution included in gross income is subject to an additional ten percent tax.

Qualified disability expenses include education, housing, transportation, employment training and support, assistive technology and personal support services, health, prevention and wellness, financial management and administrative services, legal fees, expenses for oversight and monitoring, funeral and burial expenses and other expenses to be approved by regulations and which SSI and Medicaid otherwise would not cover. These distributions can be made over the person's lifetime. The account itself cannot be utilized as security for a loan to the beneficiary.

An ABLE account may only be established for the benefit of an individual who is (i) disabled before the age of 26, and (ii) eligible for SSI or Social Security Disability ("SSD") based on disability or blindness. Alternatively, if the beneficiary meets the SSI criteria for "significant functional limitations", a disability certification by the beneficiary, parent or guardian that includes a copy of the individual's diagnosis signed by a physician may be submitted to the Treasury each year.

ABLE accounts are similar to 529 accounts and in the same manner will be maintained by the individual states or state agencies, although ABLE accounts have additional restrictions. For example, multiple 529 accounts can be established for a beneficiary who, depending on state law, may or may not be a resident of the state in which the account is established; however, only one ABLE account may be established for a beneficiary who must be a resident of the state where it is established (unless the resident state does not have an ABLE program). If multiple ABLE accounts are established, each such account established after the first account will cease to be an ABLE account and the beneficiary will be treated as having received a distribution of the assets of the non-qualifying ABLE accounts.

Similar to 529 accounts, an ABLE account may be rolled over to a qualified sibling or step-sibling and investment direction by the beneficiary is limited to two times per calendar year. Although limited, this potentially allows qualified individuals to have greater control over their resources than otherwise possible.

Whereas 529 accounts are deemed owned by the person who established it, ABLE accounts are deemed owned by the disabled individual. Upon the death of the beneficiary, any amounts remaining in the account after the payment of outstanding qualified disability expenses will be paid to the state upon it filing a claim for payment; however, the amount paid to the state may not exceed the amount of medical assistance paid for the beneficiary by the state after the time the account was established. Thus the state is a creditor of the account to the extent it has provided the beneficiary with governmental assistance after the account was established. Only after the state is reimbursed will the balance pass to the estate of the beneficiary. The reimbursement to the state is a drawback of the ABLE accounts which will likely result in the continued use of third party funded Supplemental or Special Needs Trusts ("Special Needs Trusts").

Special Needs Trusts are trusts established and funded by third parties for the benefit of a designated beneficiary to permit the beneficiary to continue to receive governmental assistance while funds are utilized from the Special Needs Trust for such expenses that governmental assistance would otherwise not cover. Upon the death of the beneficiary, the funds will pass as set forth in the Trust document and the state would have no claim for recovery. Unlike the ABLE accounts, the funds placed into a Special Needs Trust receive no income tax benefit. Special Needs Trusts are also more costly to set up and are more limited in the expenses which can be paid on behalf of the beneficiary without affecting governmental assistance.

Officers, employees or their designees having control of a qualified ABLE program will need to file reports with the Treasury detailing contributions, distributions, account balances, name and state of residence of the beneficiary and other matters. The information will be used by the Treasury to monitor the program and to a limited extent to report to the public.

States may also recognize ABLE accounts to provide state income tax benefits similar to those provided for by some states with respect to 529 plans. Massachusetts recently enacted legislation which included provisions recognizing ABLE accounts for state tax purposes.

There remain a number of unanswered questions with respect to ABLE accounts. However, in the next six months the Treasury will be developing regulations and issuing other direction. Specific cases will also provide further guidance. Issues that must be addressed and procedures to be developed by the Treasury include the following: (i) a method for allowing individuals to verify the existence of ABLE accounts to avoid a beneficiary having multiple accounts and to allow the Treasury to enforce the one ABLE account per eligible beneficiary limit; (ii) a method of maintaining the list of eligible individuals so that governmental agencies can confirm eligibility status; (iii) details with respect to information to be reported to the Treasury and any notices required to be generated; (iv) a method for processing disability certifications and determinations of disability; (v) a list of qualified disability expenses; (vi) the information required to be presented to open an ABLE account; (vii) a method for allowing transfers from one ABLE account to another; and (viii) methods to prevent fraud and abuse with respect to amounts claimed as qualified disability expenses.

ABLE accounts provide an additional option and/or an alternative to Special Needs Trusts for families wanting to provide financial assistance to members with disabilities. The ABLE Act encourages the use of private funds to provide adults with disabilities greater independence and quality of life.

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