SPECIAL NEEDS ALLIANCE

Attorneys for special needs planning.

May 24, 2022

IRS and REG-105954-20
Room: 5203
Internal Revenue Service
PO Box 7604
Ben Franklin Station
Washington DC, 20044

Re: Comments on Proposed Regulations IRS REG-105954-20
Ladies and Gentlemen:

The Special Needs Alliance ("SNA") is hereby submitting its comments regarding the proposed regulations under Section 401(a)(9) of the Code.

The SNA is a nonprofit organization of member attorneys committed to the practice of disability and public benefits law throughout the United States. SNA members are peer-selected based on a combination of relevant legal experience in the disability and elder law fields, direct family experience with disability, active participation with national, state, and local disability advocacy organizations, and professional reputation. Our 143 SNA members have an average of 18 years of relevant legal experience, with no member having practiced law for less than five years. As a result, we think we are uniquely positioned to offer comment and recommendations on the provisions of the Proposed Regulations relative to the SECURE Act's treatment of disabled and chronically ill beneficiaries and Type II Applicable Multi-Beneficiary Trusts for their benefit.

SNA's comments and recommendations are set forth in the attached memorandum. We would welcome the opportunity to discuss our comments and recommendations should the Service wish to do so. Should the Service wish to discuss, please contact Tara Anne Pleat, Esq. at TPleat@WPLawNY.com or 518-881-1621.

Respectfully submitted,

Mary E. O'Byrne
SNA President

Special Needs Alliance Comments and Recommendations

1. § 1.401(a)(9)-4(e)(4)(ii) and (iii) Alternative Methods for Proving Disability are Necessary for Adults and Minors.

§ 1.401(a)(9)-5(f)(2)(ii) states that the only "safe harbor" for proving a status of disabled is a Social Security Determination of disability for adults (for those over the age of 18). There is no other method of proof offered.

Documenting disability status for adults. The proposed regulations appear to rely solely on the Social Security Administration's findings regarding disability for adults (those over age 18) and provide no alternative path for proof. This narrow approach could prevent many individuals, legitimately disabled at the time of an employee's death, from qualifying as Eligible Designated Beneficiaries ("EDBs").

While documentation of disability by the Commissioner of Social Security is and should be conclusive proof of status, many adults with disabilities are ineligible to apply for or receive a formal determination from the Commissioner of Social Security. The most common type of disability benefit is Social Security Disability Income (SSDI), based on premiums paid through quarters of work.[1] Women, homemakers, and stay at home parents may be seriously disabled and meet the definition of disability in the statute, but fail to meet the required work record tests hence they lack a determination by the Social Security Administration. Their status should not prevent them from qualifying as EDBs if they otherwise meet the statutory criteria under Code Section 72 (m)(7). The second alternative disability benefit, Supplemental Security Income (SSI), is for those individuals who have limited income and resources and are disabled but have never met the work records tests sufficient to qualify for SSDI[2]. Applicants who do not meet the financial criteria for SSI do not progress in the application process to get a disability determination. Further, family income is "deemed" to the applicant, which may render many homemakers and stay at home parents financially ineligible, yet them may still be disabled under the SECURE Act definition of Section 72 (m)(7).

Documenting disability status of minors

As the Proposed Regulations recognize, minors do not typically engage in "substantial gainful activity" so determining disability status through this Social Security Administration adult disability criteria remains impossible for many minor plan beneficiaries. Since the Social Security Administration provides SSI benefits only for those severely disabled minors whose families fall under the strict SSI income and asset limits, most disabled minors will not receive a disability determination because their families are living above poverty level.[3]

Suggested modifications to the regulations adding another "safe harbor" for proving disability status

[1] In order to qualify for SSDI benefits, an individual must meet both the duration of work test, i.e., sufficient quarters worked to be insured; and the recent work test, a certain number of quarters worked in the most recent years, e.g., 5 out of the past 10 years.

[2] The current asset limit for SSI is $2000 in countable assets. The current income limit is $841 per month.

[3] The Social Security Administration "deems" the income and assets of the family with whom the minor resides to the minor in determining eligibility for SSI. Accordingly, SSA will not undertake a finding of disability for the majority of minors, regardless of the severity of the disability.

The SNA respectfully requests that additional methods of documenting disability for adults and minors be added to the regulations consistent with the ABLE Act regulations.

The Treasury regulations under the ABLE Act, 1.529A-2 (d)(ii) provide another "*safe harbor"* for determining disability. Specifically, the ABLE Act final regulations provide for a "disability certification" signed by a licensed health care provider described in (e)(1) of the regulations. For purposes of determining eligibility status, the filing of a disability certification will be deemed to have been made once the qualified ABLE program has received the disability certification. This parallels the SECURE Act certification of chronically ill status, which is also certified by a licensed health care provider. Other programs under state and federal benefits law recognize the need for alternative methods for determining and substantiating disability due to the limitations of the Social Security Administration's determinations explained above. Accordingly, most states provide for alternate documentation of disability through a separate state agency or state contractor based on the identical definition of disability as in the federal statutes, including the SECURE Act.

A certification of the Section 72 (m)(7) criteria by a licensed health care provider as to disability status is not only fair, but practical and consistent with the ABLE Act regulations. This certification also resolves concerns raised by retirement plan administrators and financial services firms that they are being made the deciders of disability or chronic illness status and the holders of the personal medical information upon which the disability status is based. The ABLE regulations require only that a certification of disability be filed with the account provider. The SNA believes that such a certification should also be a safe harbor for the purposes of documenting disability under the SECURE Act for adults and minors alike.

2. §1.401(a)(9)-4(e)(4)(iii) Extended Beneficiary Finalization Date should be considered for Determining a Minor Child's Disability as of the Employee's Death.

Under the Proposed Regulations, a minor's disability must be established as of the date of the employee's death, and evidence of the Social Security Administration's determination of disability submitted by October 31 of the year after the year of the employee's death. For the reasons described above for minor children disabled as of the date of the employee's death, submitting proof of early disability by October 31 of the year after the year of the employee's death may simply not be possible.

Most determinations of disability for young people by the Social Security Administration are in fact made between the ages of 18 and 21, even if they relate back to birth. Moreover, some disability determinations under the equivalent of Section 72 (m)(7) by a licensed medical provider also may not be possible for very young minors by October 31 of the year after the year of death. Finally, minor children of the employee are EDBs in any event and entitled to receive life expectancy distributions until age 21 plus 10 years.

The SNA respectfully suggests that the Treasury Department allow minor children an extended date to provide certification or proof of disability, i.e., the later of October 31st of the year after the year of the Employee/Parent's death or the minor's 21st birthday. A delayed date for proof of disability relating back to the employee's date of death would not impose a substantial hardship on financial institutions managing these accounts since the required minimum distributions (RMDs) in either case would be identical.

3. Collateral Benefits

Proposed § 1.401(a)(9)-4(g)(3)(i)(A) and (B) together provide that to qualify as a Type II applicable multi-beneficiary trust (AMBT), the trust terms must provide that no individual, other than a

chronically ill or disabled individual, has any right to the interests in the plan until the death of all the chronically ill and disabled beneficiaries of the trust. SNA respectfully requests that examples be incorporated to confirm that trust distributions that are for the benefit of the disabled or chronically ill beneficiary but paid to a third party who is not disabled or chronically ill, do not result in the loss of Type II applicable multi-beneficiary trust status and does not equate to that non-disabled or non-chronically ill third party having a right to the interest in the plan.

SNA respectfully recommends the following examples:

Example 1: A dies in 2022. A has created a Type II applicable multi-beneficiary trust for the benefit of her disabled son B which is the named beneficiary of her plan benefits. Beneficiary B is the sole current adult beneficiary of the Type II applicable multi-beneficiary trust. A's daughters S and E are the named remainder beneficiaries of the Type II applicable multi-beneficiary trust after B's death. Because of B's disability, B is unable to live alone. For B to travel, to attend family gatherings, or go on a family vacation, the Trustees are given discretion to pay for B's travel expenses and that of a companion, including a sibling, a close friend, or a direct support professional or party that is not disabled or chronically ill. These payments are for the benefit of B, because without a companion receiving a derivative/collateral benefit, B would not be able to attend family gatherings or go on family vacations. The trust qualifies as a Type II applicable multi-beneficiary trust.

Example 2: Same facts as Example 1, except Beneficiary B is chronically ill and is no longer able to perform two activities of daily living without the assistance of another person. The trust qualifies as a Type II applicable multi-beneficiary trust even though the companion is receiving a derivative/collateral benefit.

Many trusts that are drafted for disabled or chronically ill beneficiaries explicitly give the trustee discretion to use trust funds for the wellbeing of the beneficiary that may be tangentially beneficial to relatives or close friends of the beneficiary who are not disabled or chronically ill. These relatives or close friends may also be the remainder beneficiaries of the Type II AMBT. These payments do not give rise to the friends or relatives having a right to the interests in the plan benefits payable to the Type II AMBT.

For example, if due to the disability of the individual he or she would not be able to travel alone to attend a family gathering or go on a family vacation, Trustees are given discretion to pay for the disabled or chronically ill individual's travel expenses and that of a companion. The companion is often a sibling, a direct support professional or party that is not disabled or chronically ill. These payments are for the benefit of the disabled or chronically ill individual (i.e., but for the companion expense the disabled or chronically ill individual would not be able to attend), notwithstanding the fact that the third-party companion is receiving a derivative/collateral benefit.

Similarly, the trustee may be authorized to pay the beneficiary's share of expenses while living in the home of a close relative who is not disabled or chronically ill. These payments are for the benefit of the disabled or chronically ill individual, even though the funds are being paid directly to a family member or a close friend who is not.

For fiduciary income tax purposes, these payments while not made directly to the disabled or chronically ill beneficiaries are treated as distributions for the benefit of the disabled or chronically ill beneficiary. The distributions will carry out income to the disabled or chronically ill beneficiary under IRC Sections 643 and 661.

SNA wishes to draw attention to the parallel concept in the public benefits area. The Social Security Administration in the issuance of the Programs Operations Manual Section (POMS) SI 01120.201F.3 addressed collateral/derivative benefits to third parties directly in discussing the "sole benefit rule.".[4] Prior to the issuance of the POMS SI 01120.201F.3, the "sole benefit rule" was interpreted to mean that Trustees of Supplemental Needs Trusts (Type II applicable multi-beneficiary trusts) could only spend trust funds on goods and services that were solely for the benefit of the disabled or chronically ill trust beneficiary and could not provide a collateral/derivative benefit to anyone else. This "sole benefit rule" draws an easy comparison to Proposed § 1.401(a)(9)-4(g)(3)(i)(a). The Social Security Administration's updated (POMS) SI 01120.201F.3 (published in April 2018) makes clear that derivative benefits to others did not violate this rule and clarified that trust distributions need only be for the "primary benefit of" the disabled or chronically ill trust beneficiary, acknowledging the practical way these types of trusts are routinely administered both out of necessity and common sense.

4. Treasury Should Expressly Provide in §1.401(a)(9)-4(g)(3) that an Inherited IRA may be Transferred by a Disabled or Chronically Ill EDB to such Beneficiary's First Party Special Needs Trust as was authorized in Private Letter Ruling 200620025 (February 21, 2006).

In PLR 200620025 addressed a fact pattern in which the Employee's disabled son was a beneficiary of his deceased father's IRA. The son was at risk of losing his Medicaid and other public benefits because of being named as an outright beneficiary of his father's IRA. The son's mother was his guardian. She established a first party special needs trust under 42 U.S.C. § 1396p(d)(4)(A) of the Social Security Act (a "(d)(4)(A) trust") and she was the trustee of the trust. The (d)(4)(A) trust was a grantor trust under Code §§ 677(a)(1) and (2) because the son was entitled to trust income in the discretion of the trustee and the trustee could also accumulate the trust income for her son's benefit. His mother was a nonadverse party, having disclaimed her right to any portion of the trust as a potential remainder beneficiary. The ruling allowed the son's inherited IRA share to be transferred by trustee-to-trustee transfer into an inherited IRA in the name of the grantor trust. After such transfer, RMDs were taken based on the son's life expectancy. The Service ruled (i) that the son's transfer of the IRA to the trust was not a taxable sale or exchange and was not a transfer for purposes of Code section 691(a)(2), and (ii) that based on these facts, particularly the necessity of forming a special needs trust, it was appropriate for RMDs from the IRA to be calculated using the life expectancy method allowed under the law at that time.

The SNA joins ACTEC and respectfully recommends that the result of PLR 200620025 be incorporated into the final Section 401(a)(9) regulations that pertain to Type II AMBTs, using the following example:

> *Example 1*: J died before his required beginning date (RBD) in 2022. He has named his four adult sons as the beneficiaries of his IRA. His youngest son, N, was disabled as of J's death and was receiving Medicaid. N was at risk of losing his medical assistance because of being named the beneficiary of his father's IRA. N possessed the capacity to establish a first party

[4] *Available at* https://secure.ssa.gov/poms.nsf/lnx/0501120201; The POMS in its directive states in its explanation of the sole benefit rule that "the key to evaluating this provision is that, when the trust makes a payment to a third party for goods or services, the or services must be for the primary benefit of the trust beneficiary. You should not read this so strictly as to prevent a collateral benefit to anyone else…."

special needs in accordance with 42 U.S.C. § 1396p(d)(4)(A) of the Social Security Act (a "(d)(4)(A) trust"). Prior to September 30, 2023, the (d)(4)(A) trust was established by a petition to the probate court. N is the sole beneficiary of the (d)(4)(A) trust. No one other than N has an entitlement to the IRA benefits during N's lifetime. N's mother is the trustee. N's mother made a qualified disclaimer of any contingent interest she might have in the trust and is a nonadverse party because she is not a trust beneficiary. The (d)(4)(A) trust is a grantor trust under Code §§ 677(a)(1) and (2) since N is entitled to trust income in the discretion of the trustee and the trustee may also accumulate the trust income for N's benefit. At N's death, as a statutory condition of establishing a (d)(4)(A) trust, the state Medicaid agency where N resides is the primary creditor of the trust. After payment of any claim made by the state Medicaid agency, the remaining trust property, including the undistributed balance of the inherited IRA payable to N's trust will be distributed to the Secondary Beneficiaries, who are N's brothers. These Secondary Beneficiaries are all treated as Designated Beneficiaries. The court ordered the establishment of the (d)(4)(A) trust and a trustee-to-trustee transfer of the IRA benefits from J's IRA to the inherited IRA established by the trustee for N's (d)(4)(A) trust.

Analysis: N is a disabled EDB. The trust is a Type II AMBT and is allowed to determine RMDs using the life expectancy method based on N's life expectancy. N's brothers are Secondary Beneficiaries and are disregarded in accordance with Proposed § 1.401(a)(9)-4(g)(3)(ii).

A (d)(4)(A) trust requires that, upon N's death, the State or States that provide Medicaid services be named as the first creditor to recover medical assistance paid during N's lifetime. Deferring payment to the State until N's death allows the trustee to preserve resources within the (d)(4)(A) trust during N's lifetime and to be repaid after N's death, unlike other creditors that would require payment as services are rendered to N.

There should be no tax effect because of the transfer to N's (d)(4)(A) trust. Firstly, as stated in § 1.408-8(d)(4), the transfer from the father's IRA to an inherited IRA held in N's (d)(4)(A) trust is a trustee-to-trustee transfer and as such is not a taxable distribution. Moreover, allowing N's (d)(4)(A) trust to be considered a Type II AMBT is tax neutral. N will pay the same amount of taxes on the RMDs and other withdrawals from the inherited IRA payable to N's (d)(4)(A) trust as he would have if N were still the outright beneficiary of the inherited IRA because of the (d)(4)(A) trust's status as a grantor trust.