
ABLE Account

On December 19, 2014, President Barack Obama signed into law HR 5771, the *Tax Increase Prevention Act of 2014* (TIPA 2014). In addition to extending a number of popular individual and business tax provisions, the Act also added new code section 529A to the Internal Revenue Code (IRC). This code section provides for the creation of a new type of tax-favored savings account, termed an “ABLE” (**A**chieving a **B**etter **L**ife **E**xperience) account.¹

Overview

Individuals with disabilities face significant barriers to finding and holding employment and living independently because their access to safety-net programs such as Supplemental Security Income (SSI) and Medicaid can be lost once they establish a minimum level of savings and income.² ABLE accounts, similar in nature to IRC Sec. 529 plan accounts for education funding, are designed to encourage and facilitate the ability of those with significant disabilities to live and work independently, without losing the benefits of SSI or Medicaid.

Under current federal legislation, a state (or an agency or instrumentality of a state) may establish and maintain a qualified ABLE Program. In general, a qualified ABLE program must meet the following requirements:

1. Contributions may be made to an account established solely for the purpose of meeting the qualified disability expenses of the designated beneficiary of the account.
2. The program must limit a designated beneficiary to *one* account, wherever located.
3. Certain other requirements of the law. For example:
 - There must be a separate accounting for each designated beneficiary;
 - A beneficiary’s ability to direct the investment of contributions to the account must be limited to no more than two times a year.
 - No interest in any portion of an account may be pledged as security for a loan.

¹ The discussion here concerns federal income tax law. State or local income tax law may differ.

² SSI has an individual resource limitation of only \$2,000. In most states, qualifying for SSI also confers Medicaid eligibility. Generally, when SSI recipients have income and resources over the limit, their SSI benefits are suspended, but they remain eligible for Medicaid.

ABLE Account

- There must be adequate safeguards to prevent aggregate contributions in excess of the limit established by the state.

A qualified ABLE program is generally exempt from federal income tax, other than the tax on unrelated business income of tax-exempt organizations.

Effect of ABLE Accounts on Federal Means-Tested Programs

An amount in an ABLE account, or any distribution from an ABLE account for qualified disability expenses, is generally disregarded for the purposes of determining eligibility for federal means-tested programs such as SSI or Medicaid. There are two exceptions to this:

- A distribution made for *housing* expenses is not disregarded for purposes of the SSI program.
- Any amount in excess of \$100,000 is considered a “resource” for purposes of federal means-tested programs.

Generally, if a disabled individual is found to have excess resources, his or her eligibility for SSI is suspended (not terminated), but eligibility for Medicaid is unaffected.

Eligible Individual

An eligible individual is someone who became blind or disabled before reaching the age of 26. Additionally, the individual must be either (1) entitled to Social Security disability benefits or SSI, or, (2) have a physician-signed certificate of disability on file with the IRS. The certificate of disability must attest that the disabled individual is either blind or has a medically determinable physical or mental impairment which results in marked and severe functional limitations which can be expected to result in death or which has lasted or can be expected to last continually for at least 12 months.

Designated Beneficiary

A designated beneficiary of an ABLE account must be an eligible individual who is the owner of the account and who is designated at the beginning of participation in a qualified ABLE program as the beneficiary of amounts paid into the program.

Contributions

Contributions to an ABLE account are considered a completed gift of a present interest,¹ must generally be in *cash*, and are *nondeductible* for federal income tax purposes. In addition:

- On an annual basis, contributions to an ABLE account may not exceed the federal annual gift tax exclusion. For 2018 this exclusion is \$15,000.² This limit may be exceeded in case of a rollover from a prior ABLE account. Excess contributions are subject to a 6% excise tax.
- Total overall contributions may not exceed the limit imposed on accounts under the qualified tuition program of the state maintaining the qualified ABLE program.
- Tax Cuts and Jobs Act of 2017(TCJA) – The TCJA, for 2018-2025, allows amount from 529 higher education plans to be rolled over to an ABLE account, provided that the ABLE account is owned by the beneficiary of the 529 account or a member of the beneficiary's family. Such rolled-over amounts count toward the annual limitation (\$15,000 in 2018) that may be contributed to an ABLE account. Any amount rolled over in excess of this limit will be included in the beneficiary's gross income.
- TCJA also included a provision to temporarily (2018-2025) increase the amount that may be contributed to an ABLE account. After the overall limitation on contributions is reached (\$15,000 in 2018), an ABLE account's designated beneficiary may contribute an additional amount, up the lesser of (a) the federal poverty level for a one-person household;³ or (b) the individual's compensation for the year. TCJA also temporarily allows the designated beneficiary to claim the Saver's Credit for contributions made to his or her ABLE account.
- Contributions may be made by any person. The term "person" includes an individual, trust, estate, partnership, association, company, or corporation.

¹ In general, exempt from both gift tax and Generation Skipping Tax (GST).

²This amount is subject to adjustment for inflation in future years.

³ For 2018, the federal poverty level for a one-person household in the continental U.S. is \$12,140; for Alaska it is \$15,180; and for Hawaii it is \$13,960.

ABLE Account

- If a contributor makes other gifts to a designated beneficiary, in addition to the gift to the designated beneficiary's ABLE account, the contributor's total gifts to the designated beneficiary could exceed the annual gift tax exclusion and result in a gift tax liability.

Distributions from an ABLE Account

Distributions from an ABLE account to the designated beneficiary are excluded from income to the extent that they *do not exceed* the beneficiary's qualified disability expenses.

If the amount distributed *exceeds* the beneficiary's qualified disability expenses, a portion of the distribution is included in the beneficiary's income. In calculating the taxable portion of the distribution, the difference between the qualified disability expenses and the amount distributed is reduced by an amount which bears the same ratio to the distributed amount as the qualified disability expenses bear to that amount. This follows the tax treatment of annuities, as outlined in IRC Sec. 72.

An amount includable in a beneficiary's income is also subject to an additional 10% tax.

Example: Assume that a qualified ABLE account with a balance of \$100,000 (of which \$50,000 consists of contributions) distributes \$10,000 to a beneficiary who incurred \$6,000 of qualified disability expenses. Under IRC Sec. 72, one-half of the distribution (\$5,000) is includible in gross income. However, the \$5,000 otherwise includable in income is reduced by \$3,000 ($\$6,000 \div \$10,000 \times \$5,000 = \$3,000$) to \$2,000. An additional 10% tax of \$200 ($\$2,000 \times 10\%$) is also imposed on the distribution.¹

Qualified Disability Expenses

Qualified disability expenses are any expenses related to the beneficiary's disability or blindness and which are made for the benefit of the designated beneficiary, including:

- Education
- Housing
- Transportation

¹ House Ways and Means Committee Report 113-614, November 12, 2014.

ABLE Account

- Employment training and support
- Assistive technology and personal support services
- Health, prevention, and wellness
- Financial management and administrative services
- Legal fees
- Oversight and monitoring
- Funeral and burial expenses
- Other expenses identified in future published guidance from the IRS.

The proposed regulations provide that the term “qualified disability expenses” should be broadly construed to permit the inclusion of basic living expenses and should not be limited to expenses for items for which there is a medical necessity or which provide no benefit to others in addition to the benefit of the eligible individual.

Rollovers

Amounts in one ABLE account may be rolled over tax-free to another ABLE account for the same beneficiary.¹ However, no more than one such rollover may be made within a continuous 12 month period. Further, the funds must be deposited into the new ABLE account within 60 days of being distributed from the prior account. A tax-free rollover may also be made to another ABLE account with a different designated beneficiary if the new designated beneficiary is (1) an “eligible individual,” i.e. blind or disabled before age 26, and (2) a sibling (including step-siblings and half-siblings, by either blood or adoption) of the former designated beneficiary.

In addition, the proposed regulations authorize a qualified ABLE program to allow direct program-to-program transfers to effectuate a change of qualified ABLE program or a change of designated beneficiary to another eligible individual.

¹ For example, if a beneficiary moves from one state to another.

Death of the Beneficiary - Transfer to State

The proposed regulations provide that upon the death of the designated beneficiary, all amounts remaining in the ABLE account are includable in the designated beneficiary's gross estate for estate tax purposes. Further, after all outstanding qualified disability expenses have been paid, any amounts remaining in the deceased beneficiary's ABLE account are subject to a claim from the state for an amount equal to the total medical assistance (Medicaid) paid for by the state. These repaid amounts are "net" of any premiums paid from the account on, by, or on behalf of the beneficiary to a Medicaid "Buy-in" program. Any funds remaining in the account after the state has been re-paid would generally be paid to the beneficiary's estate, subject to income tax on the earnings, but not subject to the 10% penalty.

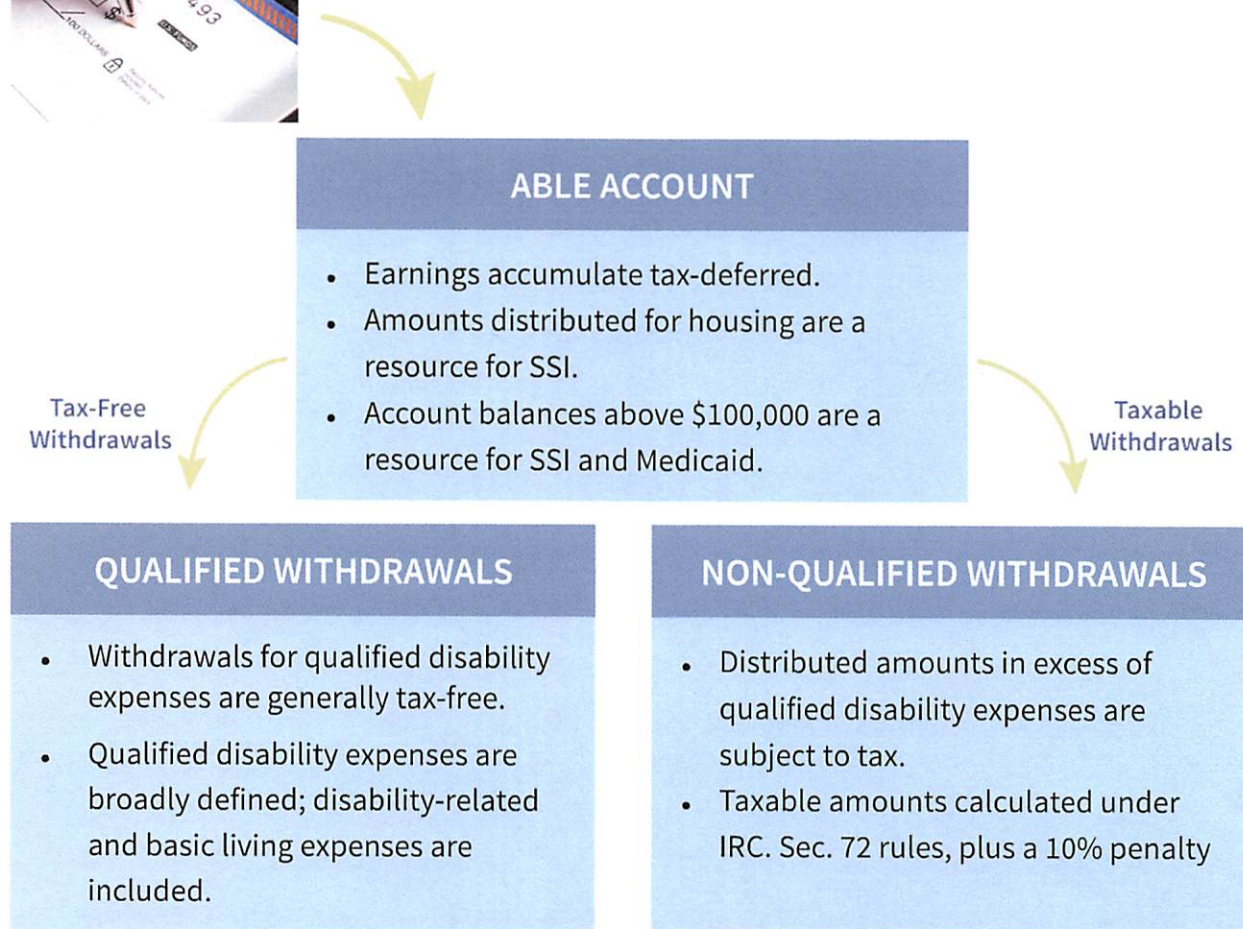
Seek Professional Guidance

The ability to establish an ABLE account represents a new option for parents or guardians to provide for the needs of a disabled individual, without jeopardizing means-tested benefits such as Supplemental Security Income (SSI) or Medicare. In deciding whether or not to establish an ABLE account, and in correctly using an ABLE account if one is set up, the advice and guidance of trained, experienced financial professionals is highly recommended.

How an ABLE Account Works

An ABLE account is a tax-favored program operated by a state designed to help parents or guardians of a disabled or blind individual pay for expenses related to the disability or blindness, without losing the benefit of means-test programs such as Supplemental Security Income (SSI) or Medicaid. Annual contributions to an ABLE account generally may not exceed the federal annual gift tax exclusion. In 2018, this amount is \$15,000.¹ The disability or blindness must have occurred before the individual reached age 26.

How Does It Work?



¹ This amount is subject to adjustment for inflation in future years. Federal income tax law does not allow deductions for contributions to an ABLE account. State or local income tax law can vary widely.