

What Attorneys Need To Know About Special Needs Trust

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ALI-ABA

What Is A Special Needs Trust?

1. Introduction

a. People with disabilities have many needs beyond basic medical care, food, clothing and shelter, including:

- i. Recreation;
- ii. Transportation;
- iii. Dental care;
- iv. Telephone and television services;
- v. Hair and nail care;
- vi. Differentials in cost of housing and shelter;
- vii. Supplemental nursing care;
- viii. Private case management; and
- ix. Mobility aids, including electric wheel chairs.

b. To provide for the payment of these needs, federal law permits a person with disabilities to retain his or her resources in one of two types of special needs trusts ("SNT") without those resources disqualifying him or her from SSI or Medicaid benefits. 42 U.S.C. §§1382b, §1396p(d)(4). The two types of trusts are:

i. d(4)(A) SNT. 42 U.S.C. §1396p(d)(4)(A). A d(4)(A) SNT is a trust created for the sole benefit of an individual with a disability under the age of 65 by the individual's parent, grandparent, legal guardian, or court. The trust must provide that the state Medicaid agency will receive amounts remaining in the trust upon the individual's death up to the amount paid under the Medicaid program for services to the individual.

ii. d(4)(C) "Pooled" SNT. 42 U.S.C. §1396p(d)(4)(C). A d(4)(C) SNT is a trust created and managed by a nonprofit organization. A separate subaccount is maintained for each beneficiary of the trust, but the assets are pooled for investment and management purposes. The account is created for the sole benefit of an individual with a disability by the individual's parent, grandparent, legal guardian, court, *or the individual*.

(1) One of the most significant differences between a d(4)(A) and a d(4)(C) trust is the ability of an individual with a disability to create his or her own pooled trust sub-account.

(2) The pooled trust must provide that to the extent that funds in the account are not otherwise retained by the trust upon the individual's death, the state Medicaid agency must receive the amounts remaining up to the amount paid by the Medicaid program for the individual.

c. The typical estate planning SNT is a Third Party SNT.

i. A Third Party SNT is a special needs trust created and funded with the assets of a person other than the disabled beneficiary. If the disabled beneficiary does not have the legal authority to revoke the trust or direct the use of the trust for his or her own support, then the trust is not a resource for SSI eligibility purposes. Therefore, a Third Party SNT should

(1) As part of their estate planning, parents and grandparents frequently create and fund Third Party SNTs for the benefit of their beneficiaries who have disabilities.

(2) The Third Party SNT affords the parents or grandparents the opportunity to preserve the beneficiary's public benefits and to supplement those benefits.

(3) In addition, the Third Party SNT provides for the proper management of the gift to the disabled beneficiary for the beneficiary's entire lifetime.

(4) At the disabled beneficiary's death, the property can pass as designated in the will or trust agreement or by exercise of a power of appointment.

ii. d(4)(A) and d(4)(C) SNTs differ from Third Party SNTs in that d(4) trusts contain the resources of an individual with disabilities and must contain a mandatory payback provision.

iii. A Third Party SNT can be created by a revocable inter-vivos trust agreement, irrevocable inter-vivos trust agreement, or a will. Ad(4)(A) or d(4)(C) SNT must be created by an irrevocable inter-vivos trust agreement.

d. Special Needs Trusts are also sometimes called supplemental needs trusts. However, the Social Security Administration refers to d(4)(A) and d(4)(C) trusts as special needs trusts. Practitioners typically refer to third party SNTs as "supplemental needs trusts" and first party SNTs, such as d(4)(A) and d(4)(C) trusts, as "special needs trusts."

e. This outline will consider and discuss d(4)(A) and d(4)(C) SNTs.

2. *Purpose.* The purpose of the SNT is to avoid:

a. The imposition of a period of ineligibility for SSI or Medicaid due to the transfer of the

resources to the trust (42 U.S.C. 1382b(c)); and

b. The treatment of the trust as a resource for SSI or Medicaid eligibility purposes.

3. *Uses and Misuses*. The following are typical situations in which an SNT is used to protect the SSI or Medicaid benefits of a disabled individual:

a. Tort recovery or settlement;

b. Inheritance (i.e., ineffective or no estate planning by the disabled individual's family);

c. Equitable distribution or alimony;

4. Due to the pay back requirement for d(4)(A) and d(4)(C) SNTs, the parents, grandparents, or other family members of a person with disabilities should not make gifts to the disabled person using a d(4)(A) or d(4)(C) SNT. They should use a Third Party SNT to make the gift. Unfortunately, in many cases, the estate planning attorney mistakenly drafts a d(4)(A) SNT or recommends a d(4)(C) SNT rather than a Third Party SNT. The improper use of the d(4)(A) or d(4)(C) SNT could result in the unnecessary repayment of Medicaid benefits to the state and a malpractice action against the estate planning attorney.

B. Is It Malpractice To Fail To Preserve SSI And Medicaid Eligibility?

1. Personal Injury Case

a. Christina Grillo settled a personal injury case in 1991 for a lump sum upon the advice of her personal injury attorney. She later sued the attorney and guardian ad litem for malpractice. She alleged that the defendants: (i) failed to consult competent experts concerning a structured settlement and (ii) failed to plan to preserve her SSI and Medicaid eligibility. Ms. Grillo alleged that a structured settlement with a d(4)(A) SNT would have protected her personal injury settlement from dissipation, provided tax benefits, and protected her SSI and Medicaid benefits. The case was settled by all defendants for a combined sum of \$4.1 million. *Grillo v. Petiete et al.*, 96-145090-92 (96th Dist. Ct., Tarrant Cty., Texas); and *Grillo v. Henry Cause*, 96-167943-96, (96th Dist. Ct., Tarrant Cty., Texas).

b. Edith Saunders, the conservator for James A. Saunders III (Jamie), settled a personal injury action on Jamie's behalf. As a part of the application to compromise and settle the claim, the conservator requested that the net settlement amount be placed in a d(4)(A) SNT for Jamie to preserve his Medicaid eligibility. The State of Connecticut objected. The Supreme Court of Connecticut rejected the attorney general's argument that the conservator should spend down all of Jamie's assets and then re-apply for Medicaid assistance. The court ruled: "By contrast, with the creation of the trust, Jamie will retain his medicaid eligibility and Saunders (the conservatrix) can provide for his supplemental needs from the trust assets, while medicaid provides for his basic medical care. Therefore, not only is the latter course of action clearly the better one for Jamie, *it may be fairly*

stated that by failing to follow it, the Probate Court, and Saunders potentially could have been deemed to be in dereliction of their duties to Jamie (italics added)." Dept. of Social Services v. Saunders, 724 A.2d 1093, 1105 (Conn. 1999). This duty requires the fiduciary of an estate and indirectly, the trial lawyer, to protect the disabled client's settlement.

2. Estate Planning

a. In 2000, an attorney was retained to draft the will that left a significant sum to the testatrix's sister who resided in a nursing home. The Medicaid program was paying for the sister's care.

b. After the testatrix's death, the sister was disqualified for Medicaid assistance, had to spend down the inheritance, and re-apply for Medicaid assistance.

c. The Supreme Judicial Court of Maine held that the attorney "could and should have drafted a 'Supplemental Needs Trust' for Robenson, thereby avoiding the Medicaid spend down...."

d. On October 25, 2002, the court suspended the drafting attorney's license to practice law due to his failure, *inter-alia*, to create the supplemental needs trust. *Board of Overseers of the Bar v. Ralph W. Brown, Esq.*, 2002 Me. LEXIS 190 (Me. October 25, 2002).

C. What Public Benefits Are Available For People With Disabilities

1. Benefits Not Based On Financial Need

a. Social Security Disability Insurance

i. An individual is entitled to SSDI benefits if he or she:

(1) Is under full retirement age;

(2) Has at least 20 credits in the 40-quarter period ending with the quarter in which the individual became disabled (20/40 rule), and is fully insured (Social Security Handbook, http://www.ssa.gov/OP_Home/handbook/ssa-hbk.htm, §207. *See* §203 for the definition of fully insured [generally one quarter for each year after attaining the age of 21 up to a maximum of 40 quarters] and §208 for a special exception to the 20/40 rule for workers disabled before age 31); and (3) Is disabled (To be disabled within the meaning of the Social Security Act, the individual must have a severe, medically determinable physical or mental impairment which has or is expected to last for one year or to result in death. In addition, the impairment must make the individual unable to engage in "substantial gainful activity." 20 C.F.R. §404.1505 for SSDI, and 20 C.F.R. §416.905 for SSI);

<(4) Files an application for benefits; and

(5) Establishes a waiting period of five consecutive months beginning with a month in

which the worker was both insured and disabled.

ii. Benefits may also be available based on the record of a living (Social Security Dependent's Benefits) or deceased (Social Security Survivors' Benefits) parent. Children who became disabled before age 22 and have remained continuously disabled may draw benefits on the record of a disabled, deceased, or retired parent as long as the child is disabled and unmarried. We often refer to such children as CDBs (Childhood Disability Benefits; formerly called Disabled Adult Child ["DAC"] benefits). ACDB beneficiary who marries another SSDI recipient generally will not lose benefits. The CDB beneficiary should contact the local Social Security Office before marrying to determine the effect of the marriage on his or her benefits and should not engage in "substantial gainful activity."

iii. SSDI monthly benefits are based on the worker's primary insurance amount (PIA), which is based on the worker's indexed monthly earnings. The worker's benefit is based on 100 percent of the PIA. ACDB of a worker is entitled to 50 percent of PIA and, if the worker is deceased, this increases to 75 percent. Spouse's benefit is also available.

iv. There are no resource or income limits for SSDI eligibility. However, if the disabled individual's earned income exceeds \$830 a month in 2005 (\$1,380 for blind individuals) (after deducting the cost of impairment-related work expenses), the person will likely not be considered disabled and therefore may not be eligible for benefits.

b. Medicare

i. Medicare is a federal health insurance program. SSDI beneficiaries are entitled to Part A Medicare benefits after 24 months (one month for a person disabled with ALS effective 7/1/2001) of qualified disability and no waiting period for people on kidney dialysis.

ii. Part A covers inpatient hospital services, home health, and hospice benefits. *It also pays for a very limited amount of Skilled Nursing Home care but not custodial care.* SSDI beneficiaries who are eligible for Part A benefits may enroll for Part B benefits but must pay a premium of \$78.20 per month in 2005. Part B benefits cover physicians' charges. Medicare generally does not pay the entire cost of hospital stays and physicians' services. In addition there are deductibles and co-pays.

iii. Under current law, there are no resource or income limits for Medicare eligibility.

c. Special Education. The federal law known as the Individuals with Disabilities Education Act ("IDEA") and related state regulations provide that a free appropriate public education will be provided to all children with disabilities, age 2 to 21 (services may be provided from age 0 to 3 by other state agencies and over the age of 21 by some states). IDEA provides that the state must provide, at no cost, appropriate public education that meets the unique needs of students with disabilities, in the least restrictive setting, which in most cases means "mainstreaming" (i.e. including) the child into the regular classroom. If no appropriate public facility is available, the education must be provided in a private school

at no cost to the parents.

i. To determine what is appropriate for the student, the local school agency ("LEA") must devise an individualized education program ("IEP") for every disabled student. The parents of the disabled student are invited to participate in the formulation of the IEP.

ii. If the parents disagree with the IEP, they may request a due process hearing. If satisfaction is not obtained at the hearing, the parents may bring suit in state or federal court.

iii. When the student reaches age 18, the parents' rights to participate in the development of and implementation of the IEP or in challenging the IEP "transfer" revert to the student, unless one of the following actions is taken:

(1) The adult student is declared legally incompetent by a court and a representative has been appointed by the court to make decisions for the student.

(2) The adult student designates, in writing, by a power of attorney, another adult to be the student's agent to participate and make decisions concerning the student's educational program.

(3) The adult student is certified as unable to provide informed consent and the LEA appoints an educational representative.

d. Civil Service And Military Survivor Benefits For Disabled Adult Children

i. Civil Service Survivor Benefits are available for an unmarried child over age 18 who is incapable of self support because of a mental or physical disability that began before age 18. The child is eligible to receive 55 percent of the parents' annuity after the parents' death. The child may receive the benefit even if a widow(er) is also receiving a survivor benefit. Children receiving a civil service survivor annuity are also eligible for federal employee group health benefits if the federal employee had family coverage at the date of his or her death. www.opm.gov/retire (U. S. Office of Personnel Management-Federal Retirees); www.opm.gov/insure/handbook/fehb29.asp (Federal Employees Health Benefits Handbook, Family Members)

ii. Military Survivor Benefits may be available if the military member selected spouse and children coverage, or children-only coverage (not automatic as the Federal Civil Service benefits are). If the member elects spouse and children coverage, the child will not receive payments until the surviving spouse becomes ineligible due to remarriage before age 55 or death. This coverage provides 55 percent of the base amount at the time of the retiree's death, divided by all eligible children. The payments end if the disabled child marries or is no longer disabled. If the child is mentally incompetent, payments must be made to a court-appointed guardian, fiduciary, or representative payee (as determined by the Defense Finance and Accounting Service) of the child. www.dod.mil/dfas/money/retired/sbg.htm (Survivor Benefits Guide); www.dod.mil/dfas/money/retired/faqs.htm (Survivor Benefits

Plan FAQ).

iii. TRICARE is a health benefit program for all seven uniformed services. TRICARE-eligible persons include active duty and retired service members and their spouses and unmarried children. Unmarried children of active duty or retired service members who have died are also TRICARE eligible. Children over 21 who are severely disabled and whose condition existed before their 21st birthday, or children whose condition occurred between the ages of 21 and 23 while they were full-time students, are eligible. www.tricare.osd.mil (TRICARE Website).

2. Benefits Based On Financial Need

a. Supplemental Security Income (SSI).

i. SSI is a federal welfare program that provides a minimum level of income for some needy persons. To be eligible for SSI a person must be:

- (1) Age 65 or older, blind, or disabled;
- (2) AU.S. citizen (with limited exceptions); and
- (3) Not a resident of a public institution.

ii. The 2005 monthly federal benefit rate for unmarried persons is \$579 and for a couple is \$869. "Deemed" income is income of another attributed to the claimant. Deeming is an issue when the minor child lives with an ineligible parent. Deeming stops applying in the month following the child's 18th birthday.

(1) Income is anything received in cash.

(2) The following cash items are specifically excluded: (A) The first \$20 of most income received in a month; (B) The first \$65 of earnings received in a month and one-half of earnings over \$65.

(3) If an SSI recipient receives items of food or shelter in kind ("ISM"), the SSA will treat the items as income dollar for dollar, subject to the lesser of the ISM provided or one-third of the federal benefit rate plus the unearned income disregard (which in 2005 totals \$213).

iii. An unmarried individual can have no more than \$2,000 of countable resources. Generally, countable resources include cash, liquid assets, and any real or personal property that an individual owns (or has the right to liquidate) and could convert to cash to use for his or her support and maintenance. 20 C.F.R. §416.1202.

iv. Non-countable resources include:

(1) A home owned and occupied by the person with a disability, or if institutionalized, in

many states, a home the person intends to return to.

(2) One automobile, if the vehicle is used for transportation for the individual or a member of the individual's household.

(3) Household goods and personal effects.

(4) Irrevocable funeral and burial arrangements. *See* POMS §SI 01130 for a list of non-countable resources.

v. Transfers of resources for less than fair market value within 36 months of an application for SSI will result in the imposition of a period of ineligibility (up to 36 months) determined by dividing the uncompensated value of the amount transferred by the federal benefit rate plus any state supplement benefit rate.

b. Medicaid. Medicaid is a joint federal and state funded program to provide medical services to the Aged, Blind, and Disabled who are needy.

i. The Department of Health and Human Services approves state Medicaid plans.

ii. The federal government provides about one-half of the funding and delegates the administration of each state's plan to the state.

(1) The individual state Medicaid programs are subject to both federal and state regulation.

(2) States have three options for the determination of Medicaid eligibility. POMS §SI 01715.010. §209(b) states use at least one eligibility criterion more restrictive than the SSI program. States that have elected this option may not use more-restrictive standards than those in effect in January 1, 1972, and must provide for Medicaid income spend down so that individuals may reduce their income to the income eligibility level. (There are 11 209(b) states: Connecticut, Hawaii, Illinois, Indiana, Minnesota, Missouri, New Hampshire, North Dakota, Ohio, Oklahoma, and Virginia.) "SSI" states use the SSI eligibility criteria for Medicaid but make their own Medicaid determinations. (The SSI states are Alaska, Idaho, Kansas, Nebraska, Nevada, Oregon, and Utah). The individual is eligible for Medicaid if he or she is entitled to at least \$1 per month of SSI benefits. §1634 states use SSI eligibility criteria and have entered into an agreement with the SSA to make Medicaid eligibility determinations. (The 1634 states are the remaining states. The agreement between the state and SSA is authorized by section 1634 of the Social Security Act, 42 U.S.C. §1383c.) The individual is eligible for Medicaid if he or she receives at least \$1 per month of SSI benefits.

iii. Benefits Provided. Medicaid provides many services that are required or desperately needed by persons with disabilities or special needs.

(1) The federal Medicaid statute requires the states to pay for certain listed medical services. 42 U.S.C. §§1396a(a)(10)(A) and 1396a-(a)(10)(C), as well as 42 C.F.R.

§§440.210, 440.220 and 440.230. These include: inpatient hospital services; outpatient hospital services; physician services; physical therapy; prescribed drugs; skilled and intermediate nursing services; home and community care for disabled individuals; community support living arrangement services; personal care services; case management services; and emergency and non-emergency medical transport.

(2) Some states have sought and have been granted special waivers to provide Medicaid services to individuals who live at home rather than in an institution. Waiver services can provide the following home and community-based services: case management; homemaker services; home health aids; and personal care services. 42 C.F.R. §§441.300 et seq. (3) State Medicaid Plans must provide for home health care for all persons entitled to nursing facility services.

c. Housing Choice Voucher Program ("Section 8")

i. Housing is one of the greatest concerns of the individuals with disabilities and their families.

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ii. Section 8 is a federal subsidy to assist with monthly housing costs.

Under Section 8 the household pays a portion of monthly housing costs based on the income of the household. This portion is usually equal to 30 percent of the household's monthly adjusted income.

iii. Subsidies are administered by a Public Housing Agency ("PHA") under a contract with the U.S. Department of Housing and Urban Development ("HUD"). PHA must conduct outreach within its jurisdiction to potentially eligible households when accepting Section 8 applications.

iv. To be eligible for the Section 8 program, applicants must:

(1) Not have income that exceeds the applicable income limit (the income limits used to determine eligibility vary by program from 30 percent of median income for the Area to 95 percent);

(2) Be a citizen or a non-citizen with "eligible immigration status"; and

(3) Be in good standing with the PHA.

v. The Section 8 Program does not specifically exempt d(4)(A) or d(4)(C) < SNTs. However, it has its own rules relating to irrevocable trusts. *HUD Handbook* 4350.3 REV-1, Section 5-7, www.hudclips.org.

(1) Generally, a Section 8 applicant must report all income earned by his or her assets or two percent per year if no income is earned on an asset.

(2) If no family member has access to either the principal or income of the trust at the current time, the trust is not included in the calculation of income from assets. Therefore, a d(4)(A) SNT should not be considered an asset if no family member who resides in the Section 8 housing is a trustee of the trust.

(3) Distributions from the trust on a recurring basis to the applicant (other than for groceries) will be considered in the applicant's annual income. Temporary, nonrecurring, or sporadic income (including gifts) is not counted.

(4) Generally, the creation of the trust is considered an asset disposition for less than fair value and the applicant must count the assets transferred to the trust for eligibility purposes for two years.

However, there is an important exception for d(4)(A) or d(4)(C) SNTs funded with the proceeds of a litigation settlement or judgment. These assets are excepted from the two-year rule.

D. What Are The Alternatives To A d(4)(A) Or d(4)(C) SNT?

1. Consider The Alternatives

a. Before implementing a d(4)(A) or d(4)(C) SNT, you should consider whether the trust is necessary. Ad(4)(A) or d(4)(C) SNT is not always necessary or the right answer.

b. The cost of creating and funding a d(4)(A) SNT or d(4)(C) SNT must be considered. In addition, the trust will incur administration expenses, including trustee's fees, attorneys' fees, investment fees, and tax return preparation fees. These costs may be excessive in relation to the amount in question.

c. The beneficiary may not need SSI, Medicaid, or Public Housing. In a New York case the court refused to order the establishment of a special needs trust because it believed that the income available to the child from the tort settlement exceeded her monthly care needs. *Matter of LaBarbera* (Sup. Ct. Suffolk N.Y. April 26, 1996).

2. Alternatives To An SNT

a. Purchase exempt resources, such as motor vehicle or home.

b. Pay off debt, including mortgages and credit card debt.

c. Prepay bills.

d. Give up needs-based benefits and rely on the individual's resources, income, and non

needs-based benefits.

e. Personal service contracts for a limited term or for life.

f. Prepayment of room and board for a limited term or life.

E. What Special Rules Must Be Considered When Drafting The d(4)(A) Special Needs Trust?

1. POMS Requirements

a. The SSA publishes the Program Operations Manual System ("POMS") as its publicly available operating instructions for processing Social Security claims. Although these instructions are not the product of formal rule making, the Supreme Court has held that the POMS "warrant respect." *Washington State v. Keffeler*, 537 U.S. 371 (2003).

b. The POMS contain an action chart to determine whether a trust is in compliance with the d(4)(A) SNT rules. POMS SI 01120.203; the Social Security POMS can be found at <http://policy.ssa.gov/poms.nsf/Inx/05011202B>. For a d(4)(C) SNT, you will want to contact the non-profit organization sponsoring the trust to ensure it complies with POMS requirements.

c. The action steps are as follows:

i. Was the trust established with the assets of an individual under the age of 65? If no, the trust does not qualify. If yes, go to the next question. (If the trust was established for the benefit of a disabled individual before the individual attained the age of 65, the exception to counting the trust as a resource continues to apply after the individual reaches age 65. However, any additions to the trust after the individual reaches the age of 65 are not subject to the transfer exception. The additions would be considered income in the month added and as countable resources in following months. For the purpose of this rule, additions to the trust do not include interest, dividends, or other earnings of the trust. *See* POMS SI 01120.203 B.1.b.)

ii. Was the trust established with the assets of a disabled individual? If no, the trust does not qualify. If yes, go to the next question.

iii. Is the disabled individual the beneficiary of the trust? If no, the trust does not qualify. If yes, go to the next question.

iv. Did a parent, grandparent, legal guardian, or a court establish the trust? If no, the trust does not qualify. If yes, go to the next question.

v. Does the trust provide specific language to reimburse the state for medical assistance paid upon the individual's death? If no, the trust does not qualify. If yes, go to the next

question.

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vi. Does the trust meet the special needs trust exception to the extent that the assets of the individual were put in the trust before the individual attained the age of 65? Any assets placed in the trust after the individual attained the age of 65 are not subject to this exception.

vii. Is the trust irrevocable? If no, the trust does not qualify.

d. Additional SSI Requirements

i. Disability Determination. There is no requirement that the disabled individual be determined disabled by the SSA before the creation of the trust. The determination may be made at the time the trust is submitted to the SSA for approval. POMS SI 01150.121.

ii. Administrative Expenses. POMS SI 01120.203 B.3

(1) Fees and administrative expenses may be paid during the life of the beneficiary as permitted by the trust document.

(2) The following expenses may be paid at the individual's death before reimbursement of medical assistance to the state: (A) taxes due from the trust to the state or federal government because of the death of the beneficiary; (B) reasonable administrative expenses such as an accounting of the trust to the court, completion and filing of documents, or other required actions associated with termination of the trust.

(3) The following expenses and payments may not be permitted before the reimbursement of the state for medical assistance: (A) payment of debts due third parties; (B) funeral expenses; and (C) payments to residual beneficiaries.

iii. Irrevocability

(1) The most common reason for the SSA to declare a d(4)(A) SNT to be invalid is the failure to comply with state trust laws regarding irrevocability.

(2) Not all states have abolished the Doctrine of Worthier Title ("DWT") that invalidates trusts for the life of an individual and then to his or her heirs. Under the common law DWT, an inter-vivos conveyance by a grantor with a limitation over to his or her heirs results in an automatic reversion and nullifies the attempted remainder to the grantor's heirs. For example, O conveys property to "A for life and on A's death to my heirs at law." In this case the disabled beneficiary is the grantor and sole beneficiary of the SNT. Therefore, as a general rule, a grantor who is the sole beneficiary retains the right to revoke the trust regardless of the statement that the trust is irrevocable. Some states have abolished the DWT, by statute. Where it has not been abolished by statute, the courts have

applied the DWT as a rule of construction of the grantor's intent rather than as a rule of law absolutely limiting the power of the grantors. *See Doctor v. Hughes*, 225 N.Y. 305 (1919), and *Bottimore v. The First and Merchants National Bank of Richmond*, 170 Va. 221, 196 S.E. 593 (1938). The Rule in Shelley's case is a distinctly different rule. The Atlanta (SI ATL01120.201), Boston (SI BOS01120.200), Chicago (SI CHI01120.201), Dallas (SI DAL01120.200), and New York (SI NY01220.200) Regional offices of the SSA have published regional instructions concerning the revocability of SNTs.

(3) For Florida, Georgia, and South Carolina, the trust must specify a particular person or entity as the residuary beneficiary. POMS SI ATL01120.201. This is a particular concern when the individual is mentally incapacitated and his heirs would be the logical residuary beneficiaries(s). In these states you may designate "my children," "my issue," or "my descendants." You may not designate "my estate" or "heirs."

(4) For North Carolina, a specific person or entity may be designated. In addition, wording such as "to my estate" or "to the heirs" is sufficient. POMS SI ATL01120.201

(5) Virginia has repealed the Rule in Shelley's Case but has not repealed the DWT. The DWT survives as a rule of construction. Va. Code Ann. § 55-14; *Braswell v. Braswell*, 195 Va. 971, 81 S.E.2d 560 (1954) and *Bottimore v. First and Merchants National Bank of Richmond*, et al., 170 Va. 221, 196 S.E. 593 (1938).

(6) West Virginia has abolished the Doctrine of Worthier Title. W. Va. Code §36-1-14a (2005). However, a federal district court has held that a d(4)(A) SNT created under West Virginia law that designates the beneficiary's heirs at law as the remainder beneficiaries is revocable and, therefore, a countable resource for SSI eligibility purposes. *Thompson v. Barnhart*, No. 2-02-CV-141 (D. Vt. July 17, 2003). The court reached this conclusion despite the fact the trust agreement clearly stated that the trust was irrevocable. This decision is very troubling since it appears to strip away the protection of state statutes that abolish the Doctrine of Worthier Title. Therefore, you should consider designating named residuary beneficiaries.

(7) In light of the difference in state laws, the draftsman should specify the state law that will govern the validity and construction of the trust. The trust should not provide for an automatic change in governing law if the trustee or beneficiary moves to another state.

(8) What should a careful draftsman do to avoid the imposition of the DWT? The draftsman should designate named vested remainder beneficiaries for the SNT. SNTs should expressly designate the persons who would be the disabled beneficiary's heirs as the vested remainder beneficiary. If the DWT is a rule of construction (rather than a rule of law) in the applicable state, the trust agreement could expressly provide that it is the grantor's intent to create a remainder interest in his or her heirs and that the DWT is not applicable to the trust.

iv. Legal authority to act with respect to the assets of the individual.

(1) The SSI POMS provide that "An attempt to establish a trust [account] by [a third party] without the legal right or authority to act with respect to the assets of the individual may result in an invalid trust. Note: This requirement refers to the individual who physically took action to establish the trust even though the trust was established with the assets of the SSI claimant." POMS SI 01120.203 B.1.e.

(2) The federal statutes state that a parent or grandparent may create a d(4)(A) trust for a disabled individual. Additionally, the disabled individual may not establish his or her trust. How do you create and fund the trust for a disabled but competent adult individual?

(3) The SSA is currently reviewing the authority to transfer the disabled individual's assets to the d(4)(A) SNTs on a case-by-case, state-by-state basis. The SSA SSI division has indicated as follows: The new POMS for the establishment of d(4)(A) SNTs are under review and should be issued shortly. Generally, a court of competent jurisdiction Special Needs Trusts 21 should have the authority to "establish" and fund a d(4)(A) SNT. (The SSA POMS requires that the court establish and not create the trust. See POMS SI 01120.203 B. 1. a.) Court "approval" of the SNT is not good enough. Generally, a parent should have the authority to create and fund a d(4)(A) SNT for a minor child. Generally, a parent will not have the authority to transfer an adult child's assets to a d(4)(A) SNT. However, SSA has approved a d(4)(A) SNT created by a parent with an initial funding of \$10 of the parent's money for an adult child ("Seed Trust"). Thereafter, the disabled but mentally competent adult child transferred her funds to the trust. According to SSA, a disabled, but mentally competent person may be the beneficiary of an SNT. Generally, a grandparent has no authority to transfer the assets of a grandchild to a d(4)(A) SNT. Generally, a guardian/conservator with specific authority from the appointing court should have authority to create and fund a d(4)(A) SNT.

2. State Requirements And Decoupling

a. There has been an increasing trend among the states to disqualify for Medicaid beneficiaries of SNTs who are SSI recipients. States will frequently impose additional requirements for d(4)(A) SNTs to qualify as an exempt resource for Medicaid eligibility.

i. SSI POMS 01730.048 states "Existence of a Medicaid trust will result in a referral of the case to the Medicaid State agency for a Medicaid eligibility decision. Explain to the individual that the Medicaid State agency

will determine Medicaid eligibility."

ii. Arizona has adopted a specific statute imposing reporting requirements on trustees and limiting the types of expenditures from d(4)(A) SNTs. Ariz. Rev. Stat. § 36-2934.01.

iii. New Mexico has ruled that a d(4)(A) SNT may not hold real estate nor disburse funds to provide shelter. New Mexico also prohibits any payments to a person with an obligation to support the trust's beneficiary, thereby eliminating the ability of an SNT to pay the

parents of a beneficiary for caretaking.

iv. Mississippi has established limitations similar to New Mexico's.

v. New Jersey requires that a d(4)(A) SNT agreement (1) contain an identification of the trust as a special needs trust established pursuant to 42 U.S.C. §1396p(d)(4)(A); (2) not contain any provisions intended to give any person or court the power to alter the form of the trust to a pooled trust; (3) specifically state that the trust is for the sole benefit of the trust beneficiary; (4) specifically state that its purpose is to permit the use of trust assets to supplement and not to supplant any benefits to which the beneficiary may otherwise be eligible; (5) specifically identify, in an attached schedule, the source of the initial trust property; (6) contain a spendthrift provision; (7) specifically state that the trust is established by a parent, grandparent, legal guardian, or court; (8) state that the trust is irrevocable; (9) specifically identify the trustee by name and address; (10) require the state be given notice of changes in trustee; (11) specifically require that the trustee comply with all state laws, including the Prudent Investor Act; (12) state that the trustee will be compensated only as provided by law; (13) specifically require the trustee to notify the state of the death of the beneficiary; (14) state that a formal or informal accounting shall be submitted to the state on an annual basis; (15) require the trustee to give advance notice of any expenditure in excess of \$5,000; and (16) require the residuary trust estate pass by intestacy. N.J. Admin. Code §10:71 - 4.11.

vi. Minnesota requires that "[a] supplemental needs trust may allow or require distributions only in ways and for purposes that supplement or complement the benefits available under medical assistance, Minnesota supplemental aid, and other publicly funded benefit programs for disabled persons. A supplemental needs trust must contain provisions that prohibit disbursements that would have the effect of replacing, reducing, or substituting for publicly funded benefits otherwise available to the beneficiary or rendering the beneficiary ineligible for publicly funded benefits." Minn. Stat. §501B.89 Sub. 2(d) (2004).

vii. Illinois and Colorado have also passed statutes that are specifically intended to provide protection for funds for disabled persons through the use of a trust and impose requirements on such trusts. 760 Ill. Comp. Stat. 5/15.1 (2005); Colo. Rev. Stat. Ann. §15-14-412.8 (2004).

b. The trust should be drafted to comply with the requirements of the state in which the beneficiary resides. The trust should include a trust amendment provision in the trust agreement to permit the trustee to amend the trust to conform to changes in the law or to comply with the rules of another state if the beneficiary changes the state of his or her residence.

3. Other Trust Provisions

a. Trustee. The appointment of a competent trustee is critical. Frequently the family will consider the money in the trust to belong to the family rather than the disabled beneficiary. In other cases, the family is not experienced with investments and public benefits.

Therefore, the appointment of a family member may result in a conflict of interest or mistakes. It is advisable to have an experienced and independent professional or corporation serve as trustee or co-trustee. You should ensure that a professional or corporate trustee is well-qualified to keep up with the public benefits rules, amend the trust if necessary to comply with those rules, disburse funds appropriately, and follow state and federal reporting requirements.

b. Prohibition of contributions after age 65. If assets are added to the trust after the disabled beneficiary reaches the age of 65, the amount added will be counted as a countable resource for SSI eligibility purposes. Therefore, consider drafting the trust to expressly authorize the trustee to refuse to accept additional contributions after the beneficiary attains age 65.

c. Trust Protector. On occasion the serving trustee may not adequately discharge his or her fiduciary duties. Therefore, the trust agreement should designate a trust protector with the authority to remove and replace the trustee.

d. Distribution Provisions. There are several available options (*See Distribution Standard for the Special and Supplemental Needs Trust*, by Cynthia L. Barrett, 14 NAELA Q. 10 (Summer 2001)):

i. To avoid having the trust treated as a resource, the trust should not direct distributions be made for the support, health, or maintenance of the beneficiary.

ii. Likewise, a discretionary support trust is unreliable. *See Third Party and Self-Created Trusts*, by Clifton B. Kruse, Jr. (ABA 3d ed. 2002). For example, in Ohio a fully discretionary trust, with no mention of supplemental needs, is a resource. Ohio Rev. Code Ann. §1339.51(D)(4) (2005).

iii. Many practitioners use a fully discretionary trust with precatory special needs language.

iv. Some practitioners use a fully discretionary trust but prohibit distributions for food and shelter. In light of the uncertainty of the future needs of the beneficiary, this may be overly restrictive in most states.

v. Some practitioners use a fully discretionary trust that specifically authorizes the trustee to provide in-kind support if the trustee deems that the beneficiary's needs will be better met with the distribution in spite of the partial reduction in SSI benefits due to the PMV rule.

e. Bonding and Surety. The trust should expressly address the issue of whether the trustee will be required to post a bond with surety.

f. Qualification and Public Accountings. If the trust is created by a court or guardian, the order establishing the trust and the trust agreement should specifically state whether the

trustee is required to qualify as trustee before a court and/or file public accountings with the court.

g. Powers of Trustee. The trust should expressly enumerate the trustee's powers.

h. Spendthrift Provision. The trust should contain a provision protecting the trust assets from the claims of the beneficiary's creditors and prohibit assignment by the beneficiary. However, since the d(4)(A) SNT was funded with the assets of the disabled beneficiary, it is a matter of state law whether the spendthrift provision will be effective against the beneficiary's creditors. A d(4)(A) SNT is funded with the disabled beneficiary's assets. Generally, whether a trust contains a spendthrift provision or not, a creditor of the settlor may reach the maximum amount that the trustee could have paid to the settler-beneficiary. If the trustee has discretion to distribute the entire income and principal to the settler, the creditors may reach all of the trust assets. *See §502 of the Uniform Trust Code and the Restatement (Third) of Trusts §58(2)*. Several states, including Alaska, Delaware, Rhode Island, and Nevada, have revised this rule to permit selfsettled asset protection trusts. Query: Can a d(4)(A) trust be drafted as a self-settled asset protection trust under the laws of Alaska or Delaware?

i. Fees, Taxes and Administration. The trust should contain express authority for the trustee to pay reasonable legal fees, care management fees, taxes, and administrative expenses from the trust.

j. Trustee Compensation. The trust should authorize the trustee to pay himself or herself reasonable compensation in accordance with a state statute or in accordance with express provisions in the trust.

k. Amendment. The trust should authorize the trustee or the court having jurisdiction over the trust to amend the trust as necessary to comply with applicable federal and state laws, regulations, and policy concerning d(4)(A) SNTs.

l. Grantor Trust Status. In light of the compressed tax rates for trusts and the beneficiary's normally low marginal income tax rate, consider drafting the trust as an intentionally defective grantor trust. See F(7), below.

F. What Special Or Unique Considerations Do Trustees Confront When Administering An SNT?

1. Notification Of The Creation And Funding Of The d(4)(A) Or d(4)(C) SNT To The SSA 20 C.F.R. 416.708.

a. Notification is required in two circumstances:

i. SSI and Medicaid recipients, and their representative payees, are under a continuing obligation to report any change in their income, resources, living arrangements, or other

conditions.

ii. The client must report the d(4)(A) or d(4)(C) SNT when he or she is applying for SSI or Medicaid. When you prepare a d(4)(A) or joinder agreement for a d(4)(C) SNT for a child who will not apply for SSI until he or she reaches the age of 18 due to parental "deeming" of income, consider giving to the parents a letter to the SSA notifying the SSA of the trust. The parents should be instructed in writing to attach the letter to the SSI application when it is filed after the child reaches age 18.

b. The failure to notify or report to the SSA can result in huge overpayment claims against the trust if the SSA becomes aware of the trust after the beneficiary has received significant SSI benefits and the SSA rules that it is a countable resource. There have been reports that there has been an increase in the number of large overpayment cases resulting from failure to notify the SSA immediately upon creation of the d(4)(A) SNT. The SSA will frequently become aware of the trust by an IRS computer check against the SSI rolls, which the SSA does constantly. If the trust is immediately reported to the SSA, corrective action can frequently be taken before the SSA has a large overpayment claim.

c. The notification can be in the form of a letter to the local SSA office which should include (i) the beneficiary's name; and (ii) Social Security number together with a copy of the trust agreement and trust records showing the receipt of funds. The letter should expressly answer all of the questions in an SSI step action chart with references to the applicable sections of the trust agreement. See POMS SI 01120.203 D. 1.

d. The beneficiary, or his or her representative payee, has the duty to report. 20 C.F.R. 416.704. However, it is a matter of good practice for the attorney to prepare and file the report. The report should be made by letter mailed to the local Social Security Administration office responsible for providing services to the beneficiary by certified mail return receipt requested. (The local office should be the SSA office for where the client lives.