

WHAT MAKES A SPECIAL NEEDS TRUST SPECIAL

Part I The Basics of Special Needs Trusts

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I. Introduction:

What is our goal: To benefit and improve the “quality of life” for persons with disabilities by maintaining eligibility for public benefits programs which may pay for medical care, provide additional monthly income or other support services. It is necessary to understand the impact of many public benefit programs in order to determine whether a special needs trust would be appropriate.

What is a Special Needs Trust (SNT)? A special needs trust, also known as a supplemental needs trust, is a trust that is used to supplement, but not supplant or replace, any benefits that the beneficiary may receive. This trust is designed for a beneficiary who is disabled and receiving means tested public government benefits. Distributions from the trust are discretionary and if done correctly are intended to supplement the beneficiary’s needs and not interfere with the public benefits.

The Omnibus Budget Reconciliation Act of 1993 (OBRA-93): OBRA 93 made significant changes to the Medicaid laws including codifying several forms of SNTs. As a result we have several types of SNTs including: Self-settled D4A disability trust, D4C pooled accounts trust and third party trusts. The D4A disability trust and D4C disability trusts are named after the statute and defined at 42 U.S.C. §1396p (d)(4)(A) and 42 U.S.C. §1396p (d)(4)(C). The trusts may be drafted as stand alone trusts or testamentary. This author prefers the stand alone trust. Each of these trusts will be discussed in detail later in the materials.

II. Some Basics Regarding Public Benefits Programs:

There are several public benefits programs to be aware of when considering the use of an SNT. The following is a list of programs that must be considered when working with a disabled person: Supplemental Social Security (SSI), Social Security Disability (SSD), Medicare, Medicaid,

HUD/Section 8 Housing, Veterans Benefits, Food Stamps and Community Mental Health Services.

A. Supplemental Security Income (SSI):

- SSI benefits are monthly cash benefits that are needs-based and provided to disabled persons who have never worked or did not work enough quarters to qualify for SSD.
- The 2014 monthly federal benefit is \$710.00.
- In order to qualify for SSI you must be disabled as defined by the Social Security Act, 42 U.S.C. §423(d) and §1382c(a)(3) as unable to engage in “substantial gainful activity.”
- In Michigan, if the beneficiary is eligible for \$1.00 of SSI then the beneficiary is automatically qualified for Medicaid.
- Countable assets cannot exceed \$2,000.00 and income reduces SSI dollar for dollar.
- The resource and income rules vary depending on whether the beneficiary is a minor. Living conditions (married or in the household or another) may also effect the monthly benefit.
- The monthly SSI may be reduced by 1/3 if others are providing food or shelter.
- The Program Operations Manual System (POMS) is the instruction manual for the Social Security Administration (SSA) workers. The POMS can be found at www.ssa.gov.
- Resources in a properly established SNT will not count as assets in the eligibility determination for SSI.

B. Social Security Disability (SSD)

- This is a monthly disability benefit based on a formula from the individual’s work history.
- This benefit is not means tested. No asset or unearned income restrictions.

- The individual must meet the same definition of disability “unable to engage in substantial gainful employment.”
- Earned income over \$1010.00 will reduce the benefit.
- After 24 months SSD recipients will become eligible for Medicare.

C. Medicare

- Medicare is a government health insurance coverage provided to everyone with sufficient work credits, who (1) reach age 65, or (2) become disabled prior to reaching age 65. Coverage is available regardless of resources or income.
- Medicare is a program that is paid for 100% with federal funds, and administered 100% by the federal government.
- For a person under 65 to receive Medicare they must establish that they are “disabled” and be eligible for Social Security Disability Benefits (“SSD”). If a person qualified for SSDI, Medicare coverage kicks in 2 years after the SSD benefit begins. (For a few types of disability, that two year wait is waived).
- Medicare coverage is divided into three categories. Coverage in each category is limited – that is there are things that are covered and things that are not, as well as co-pays and deductibles for things that are covered. Essentially, the “Parts” provide coverage of the following categories of medical expenses:
 - Part A: Hospital Coverage
 - Part B: Doctors Visits
 - Part D: Pharmaceutical Coverage
- Part C is the managed care option for Medicare benefits.
- Premiums are paid for Parts B and D, which amounts vary each year. Premiums for Part B are increased for a small percentage of “high income” beneficiaries.
- Part D coverage is likewise “means tested”, but with Part D, both the premiums and coverage in the “gaps” are based on a resource test that looks at both assets and income.

D. Medicaid

- Medicaid is the other government health insurance program.
- Unlike Medicare, Medicaid is only available to people who meet strict financial eligibility tests.
- Medicaid is financed by a combination of state and federal funds and is administered in Michigan by the Michigan Department of Community Health, and its agency, the Department of Human Services.
- Rules for Medicaid eligibility are different in each state.
- Medicaid is health insurance for the blind, disabled and low income families.
- Medicaid is means tested and has both asset and income limits.
- A person may not have more than \$2,000 in countable assets.
- Some assets are exempt which include the home, car and prepaid funeral.
- Persons qualifying for Medicaid may not have income above the poverty levels or they may be subject to a spend down.
- Resources in a properly established SNT will not count as assets in the eligibility determination for Medicaid.

E. MI Choice AKA Home and Community Based Waiver Program:

- MI Choice provides services and supports in the home or unlicensed assisted living facilities.
- There is a broad range of services including homemaker services, adult day care, transportation, personal care and others.
- The MI Choice Program provides a more significant level of care in the home for persons who medically qualify for a high level of care or would otherwise be eligible for nursing home placement.
- The eligibility rules for the MI Choice Program are more forgiving than traditional Medicaid.
- The MI Choice Program places a cap on the amount of income an individual receiving waiver services can receive and still be eligible for services. For 2014, the income cap is \$2130. There is no method for

“spending down” income to become eligible, if the applicant’s income exceeds this cap.

III. Types of Special Needs Trusts: ¹

A trust is a special needs trust if it is created for a person who is disabled or may become disabled with the intent to protect and maintain eligibility for needs-based public benefit programs. SNTs are also known by many names including: Supplemental Needs Trusts, Medicaid Payback Trusts, Self-Settled Trusts, Exception A Trust, Exception B Trust or Discretionary Trusts.

This outline is designed to explain how two types of “special” trusts are prepared and when they should be used in Michigan. Although each type of trust may be referred to by a variety of terms, for the purposes of this outline these trusts will be referred to as: first party trusts and third party trusts. The commonality between the two types of trusts discussed in this outline is that they are all used in situations where the settlor and/or primary beneficiary of the trust agreement is either already receiving means tested government benefits or is expected to receive such benefits in the future.

A. First Party Special Needs Trusts

- Purpose of Creating First Party Special Needs Trusts
 - i. The primary beneficiary of a first party trust is a person receiving or expected to receive means tested government benefits. The individual whose assets are used to fund the first party trust is also the lifetime beneficiary, hence the name “self settled.”
 - ii. A first party trust provides a mechanism that allows resources to be held in trust for the benefit of an individual receiving means tested government benefits while at the same time precluding those resources from being considered available for the purposes of determining eligibility for such benefits. Typical situations in which first party trusts are used include situations in which a person receiving Medicaid or SSI receives an inheritance, or receives an award or settlement from a personal injury action
- Key Characteristics of and Legal Basis for First Party Trusts

¹ Much of the materials contained in this section are drawn from prior writings of Amy R. Tripp and are reprinted with permission from *Advising the Older Client or Client with a Disability*, Fourth Edition, ICLE 2004, which was published by the Institution of Continuing Legal Education, 1020 Greene Street, Ann Arbor, MI 48109-1444.

- i. The first party trust is strictly a statutory creature. As a result, a first party trust, the “have your cake and eat it too” characteristic of the trust comes at a price. The reason individuals are allowed to take their own assets and place them in a trust, which trust allows the resources to be used for their needs during their life, and which resources are nonetheless considered unavailable resources for the purposes of determining Medicaid and SSI eligibility, is that the trust contains a provision requiring that upon the death of the beneficiary the state has a claim against the resources remaining in the trust for the value of the medical services provided to the beneficiary during his or her life up to the full amount of the trust residual.
 - ii. The first party trust is authorized by 42 USC 1396 p(d)(4). This obscure section of the United States Code provides two subsections which are central to government benefits planning. These sections are (A) and (C). It is common for attorneys versed in government benefits planning to refer to D4A and D4C trusts. These labels reference the statutory sections of the United States Code, which sections provide a legal basis for the two forms of first party trusts used in Michigan.
- There are Two Types of First Party Special Needs Trusts:
 1. By far the most common form of first party trust is the standard **Medicaid Payback Trust** authorized by 42 USC 1396 p(d)(4)(A) [the D4A trust]. The requirements of a valid Medicaid Payback Trust created pursuant to 42 USC 1396 p(d)(4)(A) are as follows:
 - That the individual beneficiary for whom the trust is created is under age 65;
 - That the individual beneficiary for whom the trust is created is disabled, with disability being defined as disability under the Social Security Administration standard for an individual to receive Social Security disability income;
 - That the trust be established by the beneficiary’s parent, grandparent, guardian or court order; and
 - That the trust provide that upon the death of the beneficiary “the State will receive all amounts

remaining in the trust [up to an amount equal to the total medical assistance paid . . . on behalf of the individual under a State plan. . .”

In Michigan the Department of Human Services recognizes the exclusion of assets in a D4A trust in BEM, Item 401, page 5, where it is referred to as an “**Exception A**” trust. It is significant to note that the BEM acknowledges the conservator as another individual who may create this trust (recognizing that the “guardian” reference in the federal statute is likely to refer to a guardian of the person and guardian of the estate). These arrangements are also recognized as exempt resources by the Social Security Administration under the label “Medicaid Trusts.”²

2. A second type of first party trust used in Michigan is the first party trust established pursuant to 42 USC 1396 (p)(d)(4)(C), sometimes called the **D4C trust**. The D4C trust is different from the D4A trust in that the D4C trust is created and managed by a non-profit entity in which individual disabled beneficiaries establish sub-accounts (which is why these types of trusts are sometimes called “**pooled account trusts**”). The requirements for a D4C trust are:

- That the trust is established by a non-profit association;
- That the individual beneficiary for whom the trust is created is disabled, with disability being defined as disability under the Social Security Administration standard for an individual to receive Social Security disability income;
- That the trust is managed with separate accounts, but pooled for the purpose of investment and management;
- That each account is managed solely for the benefit of the disabled beneficiary and is established by a parent, grandparent, legal guardian or court order; and
- To the extent that any funds remain in the beneficiary’s account upon the death of the beneficiary, those funds are either retained by the trust or paid to the state as reimbursement for medical assistance paid on behalf of the beneficiary under estate plan.

² Social Security Administration Program Operations Manual, Item SI 01120.200(H).

The D4C is recognized by the Michigan Department of Human Services in its Bridges Eligibility Manual, Item 401, page 5, where it is referred to as an “**Exception B**” trust.

An individual interested in establishing a D4C trust fills out a “joinder agreement” with the charity which has established the trust.

- In understanding how first party trusts are beneficial, it is important to understand that the real value of a first party trust is not just in the fact that the assets in the trust are not considered available resources, but that the act of transferring assets from the individual to the trust is not considered a penalizing event. Transfers of resources for less than fair market value by individuals seeking eligibility for SSI and Medicaid result in periods of ineligibility unless such transfers meet with certain exceptions. The transfer of resources to a properly drafted first party trust are not considered penalizing transfers. The Department of Human Services Bridges Eligibility Manual, Item 401, pages 5-7, discusses the fact there are no penalties associated with transfers to what they call **Exception A and Exception B trusts**. It is interesting to note the BEM expressly states that transfers to an Exception A trust which occur after the individual beneficiary reaches age 65 are subject to transfer (“divestment”) penalties, whereas the language regarding transfers to an Exception B trust by an individual over 65 is more ambiguous, indicating that such transfers “might be a divestment.” This ambiguity gives rise to the argument by some practitioners that individuals over age 65 may, in fact, enter into pooled account trust agreements and transfer resources to them without realizing any penalties associated with such transfers. These transfer exceptions are also recognized by the Social Security Administration in Bridges Operations Manual, item SI 01150.121, although there is no ambiguity in the language of the Social Security policy as to the funding of such a trust by a person over 65 (ie., the Social Security policy clearly indicates that funding of either a **D4A or D4C trust** by an individual over age 65 is a penalizing transfer).

- Comparing D4A and D4C Trusts

In advising clients as to which type of first party trust is best for them, the attorney should consider the following factors:

- The Cost. It is typically less expensive to establish a **pooled account (D4C) trust** than it is to create and fund a stand-alone **(D4A) Medicaid Payback Trust**.
- Trustee Selection. A beneficiary or their family is able to be involved in the selection of a trustee of a stand-alone **Medicaid Payback Trust**, whereas the charity acts as trustee of a **pooled account trust**.
- The individual or the family establishing a stand-alone **Medicaid Payback Trust** is able to name the remainder beneficiaries (which would receive distributions only upon the death of the beneficiary if the resources remaining in the trust are in excess of the amount of the lien for repayment of state services), whereas the charity is the remainder beneficiary of the **pooled account trust**.

As a result of these distinctions, it is common for individuals with smaller settlements/inheritances to take advantage of the benefits of a **pooled accounts trust**, whereas individuals with larger sums typically desire stand-alone **Medicaid Payback Trusts**.

B. The Third Party Funded Special Needs Trusts

- Purpose of Creating Third Party Funded Special Needs Trusts
 - The primary beneficiary of a third party trust is a person receiving or expected to receive means tested government benefits. The settlor of a third party trust is someone other than the individual receiving the benefits or the spouse of the individual receiving the benefits. As such, the settlor is a “third party” to the arrangement, hence the name.
 - Typical situations in which third party trusts are created include situations when parents or grandparents want to leave assets to severely disabled children or grandchildren. Settlers in these situations recognize that an outright gift to the beneficiary would cause the beneficiary to own resources which would cause them to lose continued eligibility for means tested government benefits or to be ineligible for such benefits in the future. A similar result would arise if the assets were left in trust for the beneficiary, if the trust is not a properly drafted.

- The advantage and purpose of a third party trust is to allow the settlor to make the resources in trust available to be used for the benefit of the disabled beneficiary while at the same time precluding the resources in trust from being considered available for the purposes of eligibility for means tested government benefits. This allows the resources held in trust to be used to provide amenities to the disabled beneficiary, which amenities s/he would not otherwise be able to enjoy. Said another way, the resources in the third party trust supplement but do not supplant, the benefits the disabled beneficiary receives through government programs. For these reasons, third party trusts are sometimes referred to as “**amenities trusts**” or “**supplemental needs trusts.**”
- Key Characteristics of and Legal Basis for Third Party Trusts
 - In Michigan, assets held in a properly drafted third party trust cannot be considered as available resources for an individual on government assistance. [See *Miller v Dept of Mental Health*, 442 NW2d 617; 432 Mich 426 (1989)]
 - Testators and settlors have established discretionary trusts in the expectation, justified under the established common law, that a beneficiary’s interest is not subject to the claims of creditors, including claims of the United States and of the state, because the beneficiary does not have an ascertainable interest in the assets of the trust. *Miller* 436-437
 - Further, the Department of Human Services (the Michigan agency administering Medicaid eligibility rules in Michigan) recognizes that assets held in a trust not created by the individual or his spouse are only available to the beneficiary of the trust to the extent that the beneficiary is able to either (1) direct use of the trust principal for his needs, or (2) direct that ownership of the principal revert to himself.³ Similarly, in determining an individual’s eligibility for SSI, the standard is that assets in a trust funded by a third party are not considered resources “as long as the beneficiary does not have the legal authority to revoke the trust or direct the use of the trust assets.”⁴

³ Department of Human Services Program Eligibility Manual, Item 401, page 12, discussion of “Other Trusts.”

⁴ Social Security Administration Program Operations Manual, Item SI 01120.202, discussion of “Trust Principal is not a Resource.”

IV. Drafting Issues and Differences between the Third Party Trust and First Party Trust

- **Revocable or Irrevocable Third Party Trusts:** Like any trust, a third party special needs trust may be revocable or irrevocable. At times a settlor of a third party trust may desire to make gifts to a third party trust for a disabled beneficiary and may desire to give that beneficiary a present interest through a “crummey power” option so as to take advantage of the annual gift exclusion amount. While there is no inherent inconsistency with using an irrevocable third party trust as a mechanism for making gifts of a present interest to a disabled beneficiary, it is important to recognize that if the disabled beneficiary is receiving needs-based government assistance at the time of the gift, the beneficiary’s failure to exercise a “crummey power” would be a transfer resulting in a period of ineligibility for certain government benefit programs, a result the individual would likely want to avoid. Otherwise, in most cases it appears to be an accepted practice for persons desiring to leave portions of their estate to disabled beneficiaries to establish a revocable third party trust during their life which is funded and becomes irrevocable at the death of the settlor. Alternately, first party trusts would be irrevocable in almost all circumstances.
- **Stand-Alone Trust:** In the opinion of this presenter, it is the best practice for third party trusts (and certainly first party trusts) to be stand-alone documents. The tradition of including special needs trust language within a will or as a sub-trust within a revocable grantor trust can be awkward and even problematic when the document is reviewed by agencies involved in providing benefits to the disabled beneficiary.
- **Lifetime Distributions Provisions:** Regardless of whether the special needs trust is third-party funded or first party, the key to its success as a protective arrangement is that the beneficiary has no legal right to compel any distributions. As cited earlier in this outline, this can only be achieved under Michigan law through the use of a purely discretionary trust. For whatever reason, it is a common error for drafters to confuse this language and thereby open the door to challenges by the government agencies reviewing the trust. These problems can arise in two contexts.
 - a. One problem arises where the drafter of a special needs trust includes discretionary language, along with language that is commonly associated with other types of trusts (such as a support trust or a trust with an ascertainable standard). Specifically, it is not uncommon to see documents that are intended to be special needs trusts include language such as “distributions are in the sole discretion of the trustee

for the health, support and maintenance of the beneficiary.” While such language would clearly support a petition for a determination that the intent of the settlor was to establish a purely discretionary trust, the inclusion of language like “health, support and maintenance” gives rise to ambiguity and frequently to challenges by a government agency as to the availability of the resource.

- b. Another area that can give rise to problems is language which is intended to prevent the trust from making distributions which would interfere with the beneficiary’s government assistance. Such language frequently indicates that the trustee may, in its discretion, use trust resources to supplement the services available to the beneficiary through a government program, but not supplant same. While this supplement versus supplant distinction is important for trustees of special needs trusts to understand in the proper administration of such trusts, the inclusion of this language in the trust agreement itself can frequently limit the trustee’s options and create confusion regarding the nature of the trust agreement.
- **Remainder Beneficiaries with Third Party SNTs:** In drafting a third party trust, the settlor establishing the trust is free to name any remainder beneficiaries they choose, which beneficiaries would typically receive whatever assets may remain in the trust after the death of the disabled beneficiary. The attorney drafting such documents should be aware of at least two issues:
 - The first issue is that if the person acting as trustee is also a remainder beneficiary, the document creates a conflict of interest in that the trustee of a purely discretionary trust who will receive whatever may be left in the trust upon the death of the disabled beneficiary may not be motivated to aggressively seek ways to use the trust resources to improve the quality of life of the disabled beneficiary.
 - The second issue has to do with the so-called doctrine of merger and/or worthier title. This doctrine, although statutorily abolished in Michigan pursuant to MCL 700.2719, has been raised by government agencies on occasion as a basis for attempting to reach the assets in a trust where the remainder beneficiaries of the trust are the heirs of the lifetime beneficiary. The position taken in those cases is that the interests of the lifetime beneficiary merge with the remainder beneficiary (those being the heirs of the lifetime beneficiary), thereby making the entire trust an available resource to the lifetime beneficiary. In the not-too-distant past, this issue was litigated in several cases with the ultimate result being a determination by the Social Security Administration that this rule

does not apply to Michigan. Nonetheless, in drafting a special needs trust remainder beneficiary provision, the drafter may want to consider avoiding that issue by simply naming individuals where appropriate, as opposed to “the heirs” of the lifetime beneficiary.

- **Remainder Beneficiaries with Medicaid Payback Provisions:** The same concerns apply to the remainder beneficiary provisions when drafting a proper first party trust which also requires a proper “Medicaid payback provision.” As cited above, the federal statute requires a provision indicating that “the state will receive all amounts remaining in the trust upon the death of such individual [the beneficiary] up to the amount equal to the total medical assistance paid on behalf of the individual under a state plan under this sub-chapter.” 42 USC 1396 (p)(d)(4)(A).

An interesting issue is currently unresolved in the state which arises where individuals drafting first party trusts have indicated that the state’s rights to recover applies only to medical assistance provided to the beneficiary after the creation and funding of the trust. In at least one case, the Social Security Administration has taken the position that this is an improper limitation. Until this matter is resolved, the prudent approach would appear to be drafting the document with language which does not limit the scope, but to leave that issue for argument at such time as the beneficiary dies and the state makes its claim against the remainder assets.

Special Needs Trust Requirements Summary

Trust	Established by	Funded by	Payback	Age limit	Statute
D4A	Parent Grandparent Guardian Court	Individual with disability	Yes	Under 65	42 USC § 1396p(d)(4)(A)
D4C	Parent Grandparent Guardian Court Individual	Individual with disability	Depends	If over age 65 may be divestment	42 USC § 1396p(d)(4)(C)
Third Party SNT	Anyone not the individual	Other peoples money	No	None	Common Law

Part II

The Administration of Special Needs Trusts

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I. Introduction:

A. Quality of Life Issue: What is Quality of Life (QOL)? Who defines QOL? What is QOL to a person who is terminally ill or physically disabled or developmentally disabled? Is the definition the same or different? What does QOL mean to you? Whose concept or definition of QOL is being used when making a determination about discretionary distributions from a special needs trust? The purpose of a special needs trust is to provide for QOL. Let's not forget the beneficiary in the definition of QOL. What is QOL to them and what would their definition be?

There are three purposes of a special needs trust (SNT): provide asset management, preserve public benefit eligibility, and provide for quality of life. Administration of a SNT is critical so that the intended purposes of the trust will be carried out. Administration includes education on distributions so as not to reduce or eliminate the beneficiary's public benefits. Administration of a SNT requires a working knowledge of the rules that govern Supplemental Security Income (SSI), Medicaid, and other public benefit programs including, but not limited to, Community Mental Health (CMH) Services. In addition the trustee must also consider budgeting, investing, accounting, reporting, taxation, and other fiduciary duties.

B. Read the Trust: It is extremely important to read the trust. You may think that this could go without saying but it is critical that as attorney or trustee you know and understand the terms of the SNT. Read the trust. It is amazing how something that seems very clear can have several interpretations. It is impossible to provide advice and manage the trust without knowing what the SNT says. Things to pay attention to when reading the trust are: parties, the intent of the settler, trustee's obligations, powers or powers that are withheld.

C. Read the Law: Most states have law on trusts and the trusts administration. Be aware of any statutory or regulatory provisions specifically related to SNTs or the administration. As a result of the complexity of the SSI and Medicaid Law, it is important that the trustee have an understanding knowledge and experience regarding these public benefits. The trustee will also have to know the federal and state laws that govern the beneficiary's particular public benefit program[s]. The rules that govern the SSI can be found in the Social Security Program Operations Manual (POM). The rules that govern the Michigan Medicaid can be found in the Bridges Eligibility Manual (BEM).

D. Who is the Client? Is your client the trustee, the beneficiary or a parent/guardian? Are there any co-trustees? Is there a trust protector or advisory committee, and if, so what is their role and duties with regard to the SNT. In a perfect world each party would have their own attorney. Often times one attorney is asked to advise all of the above-named parties.

E. Fee Agreements: In order to avoid conflicts make sure to have a written fee agreement that defines the service to be provided and address potential conflicts between beneficiary and trustee. The agreement should also be specific about fees and how fees are calculated and billed; specific services provided; and who is responsible for advice regarding taxes, accountings or distributions. It is important that all bills be kept current with a payback trust. The payback trust will not allow

payments for administration services until the payback obligation is satisfied. Only payment to legal services that relate to post-death are allowed prior to payback.

F. Notice to Agencies: A copy of the trust should be provided to the SSA and Medicaid office by certified mail, return receipt requested, if not already provided at settlement. It is recommended to put the agencies on notice at the time a court settles or approves the establishment of the SNT so as to bar those agencies from later rejecting the SNT.

II. Other Players:

A. Choosing the Trustee: Naming the appropriate trustee can be critical to the successful administration of the trust. The trustee may be a family member, a friend or other individual, a professional fiduciary, a bank, or another financial institution authorized to offer trust services. The beneficiary cannot serve as trustee, as this would give the beneficiary too much control over the trust property, and it would count as an "available" resource to him. An option is a co-trustee arrangement with a family member handling care issues and a professional trustee managing the funds and recordkeeping. Where no appropriate family members exist, another option is to appoint a care manager or committee with whom the professional trustee must consult and who will monitor and advise on the needs of the beneficiary.

The trustee is responsible to make sure that the terms of the trust are followed. The trustee also has a duty of loyalty to the primary Beneficiary (and, depending on the terms of the trust, to the residual beneficiaries, which may include Medicaid), has the duty to act and invest prudently, and the duty to maintain the books and records of the trust and to make sure that the beneficiary or his guardian is kept informed of the trust's administration.

- **Independent Professional Trustee:** An independent, professional trustee is generally the best choice if the trust is funded adequately to justify the cost. Because the independent trustee does not have a beneficial interest in the trust property other than the trustee fee, there can be no conflict of interest (although many clients may claim that the trustee is reluctant to make disbursements from the trust in order to protect the corpus and provide them with a larger fee.) The independent trustee can generally make better decisions regarding whether a requested distribution is for the sole benefit of the beneficiary, or provides more benefit for the family. Professional trustees are usually well equipped to make decisions based on the size of the trust and the beneficiary's life expectancy, ensuring that the trust is not depleted too quickly, although these should not be the final determining factors. It is critical to choose a trustee well-versed in the administration of SNTs and familiar with rules regarding public benefit programs, or at least one willing to learn and work with a qualified special needs attorney.

One of the negatives of a corporate trustee is they may not be attuned to the needs of the beneficiary or their disabling condition. The trust can provide for a trust advisor or advocate to watch over the activities of the trustee and to ensure that the beneficiary's needs are being met. A trust advisor or trust protector can be given the power to remove the trustee, with or without cause, and replace it with another entity, further ensuring the trustee does its job. At the least, the trust might require the trustee to hire a care manager to determine the needs of the beneficiary if there are no family members or other appropriate individuals to fill that role.

An interesting case regarding the duty of a corporate trustee to ascertain the needs of a beneficiary and utilize the trust funds to improve his quality of life is *Matter of JP Morgan Chase Bank N.A.* (Marie H.) 2012 NY Slip Op 22387, (December 31, 2012 Sur Ct, New

York County.) This case raises important questions about the obligations of an institutional trustee to a beneficiary with disabilities in administering a trust for the welfare of that beneficiary. An accounting was filed with the court for a fifteen year period through 2010. In a trust with income of almost \$250,000, only \$3500 was spent on the severely disabled beneficiary, while the attorney received approximately \$26,000 and the trustee \$52,000. Chase Bank explained the reason for failing to make distributions for the beneficiary was its "lack of institutional capacity" to determine and meet the needs of the severely disabled, institutionalized beneficiary. The judge ordered the bank to hire a certified care manager with significant experience dealing with individuals with intellectual disabilities and to file subsequent accountings with the court.

B. Trust Advisory Committee: A trust advisory committee (TAC) may consist of family, financial advisors and professional fiduciaries that can provide advice regarding the use of the trust funds. The committee may have a variety of powers, including the removal and appointment of trustees, so long as parameters are imposed to avoid creating revocable status.

C. Trust Protector: An alternative to trust committee is a trust protector. A trust protector can be an individual or an institution that has specific authority to remove and appoint a successor trustee. A common use of a trust protector occurs when a parent wishes to serve as trustee of their child's tort settlement. The parent may not have any experience regarding financial management, have creditor issues, lack necessary knowledge regarding public benefits, or misunderstand the fact that the corpus of the trust belongs to the beneficiary and not the families. A parent can serve as a trust protector in lieu of a trustee and be involved with the administration with other professional advisors.

D. Co-Trustees: One can also consider the use of a family member as a co-trustee to provide the personal side to the administration along with the professional trustee who is knowledgeable regarding public benefits, accountings and investments. Both, working together, will achieve quality of life for the beneficiary.

III. The First Meeting: It is essential that the trustee have good judgment. In addition to judgment, the trustee will need to understand the differences between the needs of trust beneficiaries with disabilities and those who are physically and mentally healthy. There are many unanswered and unanswerable questions regarding the beneficiary. What is the beneficiary's life expectancy? Is it accurate? Have we been too generous if the beneficiary lives much longer than anticipated? Or too stingy if death comes unexpectedly early? What affect have our actions as trustees had on the day-to-day health, happiness and well-being of the beneficiary and his or her family? What anticipated future medical needs might not be covered by medical assistance programs such as Medicaid? What role does the beneficiary and/or the family play in making those decisions? What about the lifestyle of family members living with the beneficiary. Have we reasonably addressed and managed the expectations of the family? How will we compensate family members or significant others for caring for a beneficiary, when many have sacrificed careers, the opportunity for health care benefits and retirement funds, and their own future dreams? How do we predict the future?

The initial communication between the lawyers, trustee, trust advisors, beneficiary, family members and significant others is the key element in creating the maximum quality of life for the beneficiary. This can also reduce disagreements and prevent accusations of fiduciary wrong-doing.

The following is a list of fundamental questions during the first meeting:

1) What is the nature of the disability?

- 2) What is the most reasonable expectation of life expectancy?
- 3) How much money will there be to manage?
- 4) How many needs are likely to be met in the future by sources other than trust funds, such as Medicaid or other family members?
- 5) Is the SNT necessary, or are other sources of funding or spending the money more effective and appropriate? If so, STOP here.
- 6) Is there a clear understanding between all competent parties regarding the ownership of the funds (i.e. the beneficiary's sole interest)?
- 7) Is there an equally clear understanding of the contribution of family members which must be taken into account - housing, care giving, loss of wages and socialization, effect of the disability on spouses, sibling, parents and significant others?
- 8) How can we view the entire situation in a manner which recognizes and, when appropriate, compensates for the contributions of all?
- 9) What will fair and adequate compensation to family members or friends be? How often will it be reviewed? What is the comparable rate for private duty care?
- 10) What gives the disabled person physical and emotional support and benefit? Does it matter that such benefit - perhaps a swimming pool or a time share unit - will also benefit others?
- 11) How will the trustee differentiate between requests for funds which solely benefit the disabled beneficiary, and those which are of greater benefit to others?
- 12) How often should requests for funds be made? Will there be a budget?
- 13) How will payments be made? Will there be direct vendor payment only?
- 14) What happens if the trustee, beneficiary and/or family simply cannot get along?
- 15) What authority will the beneficiary or family have to change the trustee, if any?
- 16) What happens to the residue of the trust, if any, after the beneficiary's death? Who makes this determination?
- 17) How do our own personal values and family experiences affect our responses to these questions, and our actions?

IV. Instructions for the Trustee:

A. Trustee Letter: A letter should be sent to the trustee that explains the fiduciary and trustee duties. Include a copy of the trust if the trustee does not already have it. The trustee instruction letter should contain the following:

1. Information regarding some basic trust principals including how to handle conflicts, self-dealing issues, and judicial intervention. Make sure the role of "fiduciary" is defined and what

that means to the trustee's ability to act, or refusal to act. Can the trustee delegate any duties?

2. Discuss the trustee's duties to the beneficiary. The trustee should have an initial assessment of the beneficiary's status and have updates provided. This author believes the trustee should have an in-person visit with the beneficiary at their home at least once a year.
3. The trustee needs information about the particular public assistance program or programs for which the beneficiary is or could be eligible for. It is helpful to provide the trustee a summary of the eligibility rules for the applicable programs.
4. The trustee needs to understand the "sole benefit" requirement and this needs to be explained and emphasized in the trustee instructions. Sometimes this is forgotten or misunderstood by family and friends who are confused by eligibility rules and have been through an emotional experience such as a very long personal injury case.
5. It is critical and very important that the trustee keep good records and document all actions. Make sure the trustee knows who they must report to, which may include the court, guardian, beneficiary, trust protectors, or trust advisory committees. Also emphasize to the trustee that they may be required to report or account to other governmental agencies.
6. Most importantly, make sure the trustee understands that *they may not distribute cash* directly to the beneficiary and make sure that they have a complete understanding of how a cash distribution will affect the beneficiary's public benefits.
7. Expectations regarding communication should also be addressed. Scheduled meetings with advisory committees need to be established. Will these be formal or informal and how often? How will distribution requests be made, and how quickly will a decision will be rendered regarding the request? How will disputes be resolved between trustee and beneficiary?

V. Distributions:

In the majority of trusts the trustee is responsible for distributions. Occasionally, a trust protector or advisory committee could have the authority to direct or request distributions. The use of a standard form can provide the trustee with the information necessary to make a decision regarding the distribution. Hopefully if the form is complete this will allow for a quicker response to the beneficiary. Once again, establish safeguards to ensure that the money does not go directly to the beneficiary but to the provider of the goods or services. Remember to report any distributions that reduce or eliminate a benefit to the respective agencies.

A. Initial Expenses and Budgeting: Every SNT case is going to be different and unique so as to suit the individual needs of the beneficiary. Initial expenses including housing, renovations, transportation, specialized medical equipment, and other one-time expenses will greatly reduce the principle that is available to generate future income. Planning should be well thought out and there is no one approach that fits. The trustee may consider the following helpful for making some of these decisions and with budgeting:

1. Get a copy of the economic damage report from the personal injury attorney if the funds are from litigation. The report should contain a realistic cost evaluation of future needs for the beneficiary. Note: this is not the same as a care plan.
2. Work with a case manager to develop a comprehensive care plan. For more detail see section on Use of Case Managers in Trust Administration.

3. Obtain financial information from the family including other assets and expenses.
4. Discuss initial purchases and expenses with the beneficiary, family and caregivers. Explain the pros and cons of the trust and the sole benefit requirement. Try to set realistic expectations early on and the requirements for disbursements. If successful this will help in building the relationship with the beneficiary and family. Also remember that with litigation, families may have been through many years of litigation and may not have been told or informed of the restrictions and rules that come with a SNT. Sometimes the family has experienced financial hardship throughout the litigation and is crushed when told they cannot access the funds or that they have to pay rent to live in the same home with the beneficiary. All these issues need to be addressed with understanding and compassion with the common theme to enhance the quality of life of the beneficiary.

B. Use of Case Managers in Trust Administration: A case manager or care manager is an unbiased third party who understands the aspects of the beneficiary's medical issues. The case manager is trained to know the local private and public resources for services and goods, as well as providers and vendors. In addition they understand the importance of preserving the public benefits. The case manager will typically make an in-home assessment and provide recommendations in the form of a care plan that includes the beneficiary's goals and objectives. They may assist with budgeting for items and services recommended in the care plan and can result in saving the trust money. The care manager also can help the family understand the trust administration issues and communicate effectively and timely with providers and the beneficiary. They can also continue to provide the trustee with an up-to-date status of the beneficiary's living conditions, safety issues, and changes in health.

C. Drafting Issues: Standards for distribution may be strict and prohibit outright distributions for any purpose that would result in the funds being deemed countable income for Medicaid or SSI. The advantage of this standard is that it provides security that the public benefits will be preserved, but the disadvantage is the trustee may be unduly restricted to provide assistance to the beneficiary that the family desires. Therefore, many SNT's have a blended standard with instructional language that provides guidance to the trustee over these issues.

D. In-Kind Income: The trust disbursement may count as in-kind income or direct income, depending upon whether the disbursement is paid outright to the trust beneficiary or to a third party for the benefit of the trust beneficiary. The better practice is to make disbursements directly to the provider. See 20 CFR 416.1120, et seq. Social Security Programs Operations Manual (POMS), which also provides instructions for the employees on the treatment of SNT distributions. Please note that the POMS do not have the force of law but are guidelines regarding the application of the law. The POMS can be found on the Social Security Administration website at <http://www.ssa.gov>.

E. Housing Distributions: The first thing always on the top of the list for distributions is the house. Who should own the home: the trust, the beneficiary, or joint with the family? If the trust is owned by the payback SNT, it is subject to loss at the beneficiary's death to repay Medicaid. If the trust owns the home, other family members may be forced to pay rent to the SNT and this could create financial hardship for the other family members. Therefore, it can be an advantage for the home to be owned by the beneficiary individually and a lesser interest owned by the trust and the parents, or spouse, along with a remainder interest owned by the parents or spouse to avoid the Medicaid payback and estate recovery.

F. Sole Benefit Rule: Complying with the sole benefit rule is another challenge for the trustee. The biggest issue is the house and whether other members of the household must pay rent and, if

so, how much. A fair market analysis should be completed and pro rata contributions can then be made by the household members. However, if the family is providing extraordinary care for the beneficiary this may negate the rent issue. The trustee needs to be careful when developing this strategy and consider using a professional care plan which can document the extraordinary services that the family members provide and place a fair market value on those services in order to reduce or eliminate the rent. The trustee needs to remember to distinguish between ordinary care that parents would have to provide and extraordinary services. These services could equal cash rent paid to the SNT. Also note that a parent's duty to support and provide ordinary care ends at age 18.

G. Housing and Food for SSI Beneficiaries: The trustee should never make a direct cash distribution to an SSI beneficiary as this will result in a dollar-for-dollar reduction in the SSI benefit until there is no SSI monthly benefit remaining. This can also result in the loss of the Medicaid benefit, which is often the key benefit linked to the SSI.

Social Security defines "in-kind" income as goods or services paid for directly by the trust to the provider. If the trustee distributed \$300.00 cash to the beneficiary, the beneficiary's SSI benefit would be reduced dollar-for-dollar by that amount, minus the first \$20.00 which is disregarded ($300.00 - 20.00 = 280.00$). However, if the \$300.00 were paid directly to the providers or a third-party it would not reduce the benefit. Even payments made to providers or third parties for food or shelter are considered in-kind support and maintenance (ISM) and reduce the SSI benefit. There is cap called the "presumed maximum value" (PMV) that applies to in-kind distributions for food and shelter and is set each year equally at one-third of the federal benefit rate. See POMS at SI 01120.200, et al. Capital renovations (including, but not limited to, retro-fitting) to a home do not count as an ISM, as SSA views these expenditures as increasing the value of the home. This is not the same as the SNT paying for shelter expenses, which does not increase the property value but is considered maintenance. (See POMS SI 01120.200E.1.c)

H. Other Disbursements that should be considered:

1. Health Insurance: The trustee may want to consider purchasing private health insurance or a Medicare supplemental policy. This may reduce the amount of Medicaid benefits paid out over the life of the beneficiary or may eliminate the need for Medicaid. Note: Before eliminating Medicaid consider all other CMH benefits that are available to a Medicaid beneficiary. The private health insurance may provide better and broader options for care and quicker responses for the services. These decisions are all contingent on an analysis of the medical needs of the beneficiary, size of the trust, life-expectancy of the beneficiary, and the availability of non-trust resources.

2. Life Insurance: The trustee may also consider purchasing life insurance for a family member caregiver. The loss of the family caregiver can be financial hardship on trust resources. The beneficiary should be the trust in order to comply with the sole benefit requirement if using trust funds to pay the premiums.

I. Parental Duty of Support: There is a parental duty of support that a parent has to provide basic support for a minor child. The SNT trustee may not pay for basic support otherwise owed by the parent; however, the parents have a duty to provide support for their minor child consistent with the family's historical standard of living

J. Disbursements at the Death of the Beneficiary: There are limitations on payments after the death of the beneficiary of payback trust. The following expenses may be paid prior to satisfying the payback obligation: Federal and State estate taxes and administration fees for the trust estate associated with completing the administration of the trust. Please note that funeral expenses are not allowed until after the payback obligation is satisfied. (See SSA Emergency Memo, EM-01085,

dated May 14, 2001 and POMS SI 01120.203 B.1. and SI 01120.203 B.2.g). The trustee should purchase a pre-paid funeral arrangement so as to avoid this issue. In fact, it may be considered malpractice of the trustee not to have a pre-paid funeral. In addition, professional fees should be paid as they accrue so as to eliminate any uncompensated services after the death of the beneficiary. This should be provided in writing to the trustee.

VI. Accounting Requirements:

The trustee needs to keep good records and provide accounting information to the appropriate designated persons or entities. Even if the trust does not require accounting, the trustee should do it anyway. There is always the possibility it will be required in the future. The trustee may also be required to account to the government entity that is providing a public benefit (SSI or Medicaid). There is one school of thought to provide annual accountings to the state agencies regarding disbursements made for that period in order to bar later objections. The other thought is not to file until requested so as not to provoke problems.

VII. Funding, Taxes and Investments: The trustee will usually not be involved in the initial funding of the trust, other than to receive the funds. Should the trustee refuse to accept funds without proof that the liens have been resolved? The trustee must understand the difference between a self-settled trust and third party discretionary trust and not allow funding that will jeopardize the trust and the beneficiary's eligibility for benefits.

The trustee should be advised to retain competent investment advice. The trustee may be subject to the prudent investor rule. A special needs beneficiary may have different expectations and needs as compared to a beneficiary of a spendthrift trust and, therefore, the prudent investor rule may have been disabled under the terms of the trust. It is recommended that the trustee obtain an independent analysis of the investments.

The trustee's liability should also be discussed to assure that the trustee understands the difference between trustee's actions in a representative capacity and individually. Explain the prudent person standard and its application. Advising a trustee of a SNT is challenging and requires knowledge and skill to provide those services so as to provide competent representation. When in doubt associate with someone with experience in this area. This is a specialized area of the law which requires a great deal of knowledge of public benefits.