

I. Special Needs Trust First Party Planning - Overview

If a person with a disability receives assets (typically from an inheritance, litigation recovery, or life insurance policy) while at the same time receiving needs-based public benefits (e.g., Supplemental Security Income (SSI) and Medicaid), the benefits recipient will lose his or her public benefits unless something is quickly done. In 1993, Congress reacted to this situation by authorizing the use of first party special needs trusts (SNT). The two types of first party SNT in use in California are the (d)(4)(A) SNT and the Pooled SNT. First party SNTs have numerous federal and State requirements that must be followed when establishing and administering these trusts. It is often very expensive to establish and administer first party SNTs and in some circumstances it is not cost effective or practical.

FOR EXAMPLE If a litigation settlement only nets \$10,000 and the person with a disability has capacity, it might be prudent to spend the money on an exempt asset (like an automobile) to eliminate incurring the costs associated with establishing and administering a SNT.

There is often no one right answer. Sometimes two clients will have identical fact patterns and one will opt to purchase an exempt asset and the other will opt to establish a first party special needs trust. It is up to the practitioner to provide the available options and allow the decision maker to decide which option meets his or her needs.

II. The Planning Solutions Available to a Person with a Disability Who Receives Assets

The solutions that a person with a disability has upon receipt of assets are the following:

- Do nothing and lose “needs-based” public benefits until assets are spent to below \$2000;
- Give the assets away and lose his or her “needs-based” public benefits for a period of time;
- Spend down assets in the month of receipt on exempt assets or other qualified expenditures until assets are below \$2000;
- Modify disqualifying inheritance trust into a third party special needs trust;
- Place assets in a first party (d)(4)(A) SNT;
- Join a Pooled SNT; or
- Some combination of the above.

III. Facts Needed For First Party SNT Planning

To establish a first party (or self settled) special needs trust (SNT) the practitioner must first understand the facts and circumstances of the person with a disability’s life and how they fit into the tapestry of laws that authorizes the establishment of a first party SNT. When a person with a disability receives assets (whether from a judgment, settlement, sale of property, inheritance, gift or otherwise) it is generally possible to preserve that individual’s eligibility for needs-based benefits by either establishing a (d)(4)(A) SNT (sometimes called a payback SNT) or in joining a pooled SNT (sometimes called a (d)(4)(C) SNT)). The facts the practitioner should determine include:

- **What is the person with a disability’s age?** The available options are different depending on whether he or she is under 18 years old; over 18 and under 65; or 65 and older.

- Does the person with a disability have the **capacity to execute a power of attorney**? Different options are available to a person with a disability who has the capacity to execute a power of attorney than are available to a minor or person with a disability who lacks capacity. If the individual also has a living parent or grandparent who is willing and able to assist then a relatively simple procedure exists to establish a (d)(4)(A) SNT. If he or she has no living parent or grandparent then a court petition is required to establish a (d)(4)(A) SNT. A pooled SNT may be joined in this circumstance without the need of a parent, grandparent, or court's assistance.
- **If the person lacks capacity, where are the assets coming from?** The type of procedure available varies depending on whether the source of the assets is the settlement or judgment in a lawsuit, or some other source, such as an inheritance or a gift.
- **If the person lacks capacity, is that person conserved?** If the person is conserved then a procedure exists to establish a SNT.

IV. Considerations in Choosing Pooled SNT

Important questions to consider when evaluating pooled SNTs include:

- **Is there a population in which the pooled SNT specializes?** Some pooled SNTs are restricted to serving specific populations or have developed different strengths. For example, one pooled SNT will only accept the developmentally disabled and individuals with traumatic brain injury. Another pooled SNT has a background in assisting individuals with mental illness and provides extra benefits to that population without additional cost.
- **How are distributions made?** A pooled SNT may require a committee to determine if a distribution can be made and may take days to complete a distribution request. At least one pooled SNT accepts distribution requests only in writing.
- **Is there a minimum amount required to join?** A pooled SNT may have a minimum amount it will accept in funding. Also, the minimum amount may incur a flat fee different than the normal fee schedule.
- **How are investments made?** A pooled SNT often hires a professional financial planner to invest assets. Is this fee separate or included in the pooled SNT's annual fee? What types of investments are being made and how does the pooled SNT monitor these investments?
- **What is the disposition of remaining funds?** Different pooled SNTs may pay different amounts to the State Medicaid agencies based upon amounts left to non profit association. Also, some pooled SNTs allow distributions to heirs, selected by the disabled person; of any funds remaining after the State Medicaid agency is paid.

A. Complete Joinder Agreement

The procedure for joining a pooled SNT is generally straightforward. The benefits recipient will complete a "joinder agreement" to become part of the pre-existing pooled SNT. There is often a fee to join the pooled SNT, typically between \$500 and \$2500. Some pooled SNTs require the beneficiary be represented by counsel to review the joinder agreement and advise the prospective pooled trust member of all the available options prior to allowing a benefits recipient to join.

B. Administrative Fees of Pooled SNTs

The fees for operating a pooled SNT tend to be large. It is imperative that the benefits recipient understand the fees so there are no surprises after joining a pooled SNT. The annual administration fee varies between pooled SNTs. It may be a flat fee or a fee based on a percentage of the assets under management. Counsel should inquire carefully into the fees charged by the pooled SNT and ask whether the administrative fee includes the financial management fees or whether that fee is supplementary. The practitioner should also learn whether there are any special fees such as fees for preparation of tax returns, fees for distributions made within 24 hours, or other fees for services.

V. Spend Down of Assets – Situations When Used

An individual may spend down his or her excess assets to pay for exempt assets and services and remain qualified for needs-based public benefits. This is generally not the most popular approach in planning for a person with a disability. An effective spend down will spend all of the person's excess resources down to below \$2000 in the calendar month of receipt. While the person with a disability will derive some benefit from the spending of assets in the month of receipt and be able to preserve needs-based public eligibility, he or she will have lost the future use of the assets to pay for any special needs. In most circumstances, a SNT is the preferred method of planning.

The typical scenarios where spending down assets is effective is when a person with a disability is as follows:

- When the amount of assets received is small or modest. If a relatively small amount of assets is received, spending down through the purchase of exempt assets may be the most logical course of action. Depending on the amount of assets received, the purchase of a home or vehicle such as a specially-equipped van with a lift may be considered. Televisions, clothes, and computers are also popular spend-down items.
- Over 65 year of age. A (d)(4)(A) SNT is not allowed for someone 65 years of age or older. While a Pooled SNT may be of some value for someone over age 65, if the person is in a nursing home or is likely to need nursing home care soon, a Pooled SNT typically will not work.
- When the person with a disability owns a home. The assets can be used to pay for additions and modifications to the home.
- When there are substantial debts that need to be paid off. The assets can be used to pay a home mortgage or pay off other legitimate debts of the person with a disability.

VI. Hypothetical One

A personal injury attorney calls stating he is settling a lawsuit for his client who was rendered quadriplegic in an automobile accident. The settlement is in the amount of \$100,000. The disabled client is receiving SSI/Medicaid, is 25 years old, clearly has capacity, and has a parent alive and willing to assist.

Quick Answer: Establish a (d)(4)(A) SNT with a parent “seed trust” SNT and Power of Attorney authorizing parent to fund the SNT.

Hypo 1A: Same facts, but the settlement is only in the amount of \$10,000.

Consider a spend down. Not likely to ever do a Pooled SNT in this circumstance unless parent or grandparent refuses to participate.

VII. Hypothetical Two

An attorney calls stating he is settling a personal injury lawsuit in the amount of \$1,000,000 for his client who has Prader Willi Syndrom and is qualified to receive SSI/Medicaid. The plaintiff clearly has capacity. The plaintiff is 25 years old but does not have a parent or grandparent alive.

Quick Answer: In California establish a (d)(4)(A) SNT with a Power of Attorney Petition through Probate Code Section 4541. Outside California, find procedure to have court “establish” (d)(4)(A) SNT. May consider a Pooled SNT but administrative costs would be prohibitive.

Hypo 2A: Same facts but the settlement was in the amount of \$45,000.

In this scenario, a Pooled SNT may be a viable alternative. The costs of court petition for a (d)(4)(A) SNT makes it unattractive. Consider spenddown (amount may be difficult to spend down immediately).

Hypo 2B: Same facts but the settlement was in the amount of \$5,000.

In this scenario, a spend down of assets

VIII. Hypothetical Three

An attorney calls stating he is settling a lawsuit for his client who is disabled with a traumatic brain injury. The attorney’s client lacks capacity but has a parent alive and willing to assist.

Quick Answer: In California must use Probate Code Section 3600 procedures to have court established SNT, no conservatorship or guardianship is required.

Outside California, use procedure to have court “establish” and fund (d)(4)(A) SNT. This may require a conservatorship or guardianship.

IX. Hypothetical Four

An attorney calls stating he is settling a lawsuit for his client who is 8 years old. The child has been diagnosed with mild mental retardation but his prognosis is that he will be able to attend school and work when he is old enough.

Quick Answer: Due to the uncertainty, it might be wise to have the funds transferred into a normal guardianship account for the minor. (In California a Probate Code 3611(g) trust would be recommended). It appears that a First Party SNT would not be required in this circumstance.

Keep in mind that at age 18 (typically when parent to child deeming ends), there is an opportunity to establish the (d)(4)(A) SNT by the “seed trust” approach or in joining a Pooled SNT.

Hypo 4A: Same facts, but child has severe disabilities. In California, a Probate Section 3600 (d)(4)(A) SNT would be established. Outside California, whatever court procedure is used to establish SNT should be used.

X. Hypothetical Five

An attorney calls stating that a lawsuit on behalf of his disabled incompetent client who receives SSI/Medicaid has settled. The terms of the settlement are \$100,000. The entire net settlement has already been used to purchase an annuity. The annuity pays out \$300/month directly to the disabled client who lacks capacity.

Response: This is bad and based on an actual case. The structure in this case will cause a reduction or even loss of benefits. The benefit to the person with a disability is only \$20 a month; (after \$20 income exclusion reduction of SSI dollar for dollar). To maximize the use of the

settlement, the only solution is to go back into court and unwind the settlement so that (at a minimum) the payments are made directly into a (d)(4)(A) SNT. This may be cost prohibitive. The point to this hypo is that personal injury attorneys are often advised by structured settlement salespeople to over fund an annuity. This is a problem. Annuities are inflexible. Most persons with disabilities require flexibility in the use of the money. It is recommended that the client speak with an experienced financial planner in the use of structured settlements. The financial planner can explain the risks/rewards of annuity planning next to a well balanced portfolio. Generally, a structure may be used for a portion of the settlement and the remainder is invested in equities.

XI. Hypothetical Six

A conservator comes to attorney's office. The conservatee, a 55 year old man with severe autism has just received a \$40,000 inheritance. She wants to know what to do to preserve benefits.

Quick answer: Can establish a (d)(4)(A) SNT through a court petition. In California, use Probate Code 2580 Petition.

XII. Hypothetical Seven

A 45 year old disabled person comes to the attorney's office. He received an inheritance of \$100,000 in a discretionary spendthrift trust with a distribution standard for his health, education, maintenance, or support. He recently was informed that he lost his SSI/Medicaid.

Quick Answer: This type of trust is a disqualifying third party SNT. This trust must be reformed (or modified): There are two alternatives:

- Modifying or reforming the trust back into a third party SNT, this may be possible based upon the intent of the settlor and the language of the trust. In California, a Prob Code Section 15409 petition would be filed;

- Modifying or reforming the trust into a (d)(4)(A) SNT. This would also require a petition to the court to add the necessary requirements, including a payback provision, modifying the distribution standard, and ensuring it is for the sole benefit of the disabled person.

XIII. Hypothetical Eight

A 67 year old disabled person comes to the attorney's office. He has just received a \$50,000 outright inheritance from his brother. He is competent.

Quick Answer: He is over 65 so a (d)(4)(A) SNT will not work. There may be an option to transfer assets into a Pooled SNT if the 65 and over year old person is not living in a skilled nursing facility (or expected to soon be in a facility). Pooled SNTs have no age requirement. Also, the person can sign the joinder agreement as he has capacity. However, some States (including California) state that a transfer penalty will apply for Medicaid, if the recipient is in a skilled nursing facility as they do for any senior. If there is a skilled nursing home situation, a spend down will need to be done.

XIV. Hypothetical Nine

A 67 year old disabled person along with his primary caregiver comes to the attorney's office. She has just received a \$50,000 outright inheritance from her brother. She is incompetent and has a conservatorship over her person and estate. She is living independently and is in good health.

Quick Answer: Same problem as hypo above, a (d)(4)(A) SNT will not work. However, in this case, joining a Pooled SNT will require court approval. Provided the right set of circumstances, some courts will have no problem authorizing the joinder into a Pooled SNT, and some have big problems with it. The other options include spending money on care until spent down or convincing court to do Medicaid planning