The Most Basic of Special Needs Trust Presentations: 10 Questions and Answers

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1. What is the Purpose of a Special Needs Trust?

The overarching purposes of special needs trusts are to maximize resources for and to protect the assets of individuals with disabilities. Assets may be transferred to a special needs trust from a third party or from the beneficiary himself or herself, and the trust assets and income are administered by a trustee to improve the beneficiary's quality of life. If drafted and established correctly and then administered responsibly, the existence of the trust assets will not make the beneficiary ineligible for means-tested public benefits.[1] The beneficiary continues to receive the benefits and, at the discretion of the trustee, has access to the trust assets to cover additional needs.

A special needs trust is designed to "supplement, not supplant," means-tested public benefits. A special needs trust does not supplant benefits which the individual with disabilities receives or for which he or she is eligible. Instead, assets in a special needs trust are available to supplement the beneficiary's needs not covered by benefits. As a result, special needs trusts are sometimes referred to as supplemental needs trusts. For elder law attorneys, these terms are generally interchangeable.

Most special needs trusts fall into one of two categories; they are either first party trusts or third party trusts (discussed more in Section 6, below). The purpose of a first party trust is to receive and administer assets and income of the individual or assets and income to which he or she was entitled. Those include but are not limited to litigation proceeds from a personal injury settlement or workers' compensation award, a bequest or gift from a parent, grandparent, or other caring friend or relative who did not know about or have the opportunity to create a third party trust, divorce settlements including alimony or property division, and child support payments when a child of divorcing parents has special needs. The purpose of

[1] Appendix A is a Fact Sheet published by the San Francisco Regional Office of the Social Security Administration. https://www.ssa.gov/sf/FactSheets/aianssavsssifinalrev.pdf. It includes a helpful chart comparing Supplemental Security Income (SSI) which is a *means-tested* program from Social Security benefit programs which are *non-means-tested*. The Fact Sheet refers to SSI as a "needs-based" program for people with limited income and resources which also takes into account where and with whom the individual lives. The Fact Sheet refers to SSDI as an "entitlement program" for which the individual qualifies because the individual (or his or her spouse or parent) contributed through federal payroll taxes imposed on employees and employers to fund these programs. There are many other means-tested programs and non-means-tested programs, as discussed in Section 3, and this article will use those terms rather than needs-based or entitlement to distinguish them. A special needs trust is only necessary to protect eligibility for means-tested public benefits.

a third party trust is to receive and administer assets that previously were owned or controlled by someone (a third party) other than the individual with disabilities.

2. When Might a Special Needs Trust Be Considered?

The first step in evaluating whether a special needs trust should be considered is to determine if the intended beneficiary of the trust has a disability. For special needs trust purposes, the standard used by the Social Security Administration (SSA) to define disability is as follows:

> …an individual shall be considered to be disabled for purposes of this subchapter if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than twelve months.

42 U.S.C. § 1382c(a)(3)(A).[2]

Is the individual receiving Supplemental Security Income (SSI) or Social Security Disability Insurance (SSDI)? If so, he or she meets the disability criteria (although the special needs trust may not be necessary with SSDI, see Section 3, below). If the individual is not receiving those benefits, determine whether he or she would qualify before advising the creation of a trust. The trust may be necessary to qualify the individual financially for means-tested benefits like SSI and Medicaid. If the beneficiary does not meet the disability criteria, it is unlikely that a special needs trust is appropriate.

3. Which Public Programs Are Protected with a Special Needs Trust?

This is the second question to consider when determining whether a special needs trust is appropriate. If the individual meets the disability criteria discussed in Section 2, the next step is to discern whether the individual is currently receiving or would be eligible to receive benefits that are only available to an individual who has limited assets, income or both.

Public benefit programs can be classified into two types: non-means-tested programs and means-tested benefits. Making the determination of which type of benefit the beneficiary is or could receive is important because a special needs trust is only necessary to protect eligibility for means-tested public benefits.

Appendix B is a Checklist of Benefits. A trustee administering a special needs trust or an attorney being consulted about the possible creation of a trust should have complete information about all benefits for which the beneficiary or intended beneficiary is or may become eligible.

a. Non-Means-Tested Programs

[2] The disability standard for a child is different than that of an adult: "An individual under the age of 18 shall be considered disabled for the purposes of this subchapter if that individual has a medically determinable physical or mental impairment, which results in marked and severe functional limitations, and which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than 12 months." 42 U.S.C. § 1382c(3)(C)(i). *See also*, 20 C.F.R. § 416.924.

The most common public benefits that are non-means-tested are Social Security old age, survivors, and disability insurance (OASDI), Medicare, and VA compensation. These benefits do not impose financial eligibility requirements. Eligibility for the benefits depends on other factors, e.g. work history, military service, etc.

i. Social Security Old Age, Survivors, and Disability Insurance (OASDI)

There are three categories of Social Security OASDI benefits: retirement benefits, survivor benefits, and disability insurance (SSDI).[3] These are cash benefit programs generally available to people who have worked long enough to have accrued "quarters" or credit in the Social Security system. The program is financed by employer and wage contributions in the form of payroll tax. The amount of benefit an individual receives is based on the person's contribution through payroll taxes and work history. To be eligible to receive Social Security retirement benefits, the individual must be age 62 or older. To be eligible to receive SSDI benefits, the individual must be blind or disabled. Disability is defined as "…the inability to engage in substantial gainful activity as the result of a medically determinable physical or mental impairment…"

In certain circumstances, a person may receive Social Security benefits based on the earnings of a spouse, parent or child.

ii. Medicare

Medicare is a public health insurance program that provides medical costs for doctor's visits, hospitalizations, and some in-home care and skilled nursing services.[4] To be eligible to receive Medicare benefits, the individual must be 65 years or older or have received SSDI for at least two years.

iii. VA Benefits

The U.S. Department of Veterans Affairs (VA) provides benefits to veterans, surviving spouses, parents or children of a deceased veteran, and the dependents of a disabled veteran. VA benefits that are non-means-tested include disability compensation, dependence and indemnity compensation (DIC), and various other programs such as nursing home and long-term care benefits, education benefits, vocational rehabilitation, health benefits, etc. Disability compensation compensates the veteran for his or her loss of income due to a disability incurred while in active duty service. Dependence and indemnity compensation (DIC) is a monthly income paid to a deceased veteran's surviving spouse, children or parents.

Since qualifications for Social Security benefits, Medicare and VA compensation are not based on the amount of resources or income a person has, it does not matter if the individual receives additional assets. Therefore, a special needs trust may not be necessary for an individual receiving only these benefits.

b. Dual Eligible

[3] The law is found at Title II of the Social Security Act, 42 U.S.C. § 401 et seq. and 20 C.F.R. § 404 et seq.

[4] The law is found at Title XVIII of the Social Security Act, 42 U.S.C. § 1395 and 42 C.F.R. § 405 et seq.

Keep in mind that receipt of non-means-tested benefits does not necessarily mean that the individual is not receiving means-tested public benefits. Some individuals are "dual eligible." Some states provide Medicaid to individuals whose SSDI income (or other income) exceeds the SSI limit ($733 in 2016) but is below the federal poverty limit ($990 in 2016), provided the individual has limited assets. Some individuals may have sufficient work history to receive some SSDI but not up to $733. In those cases, if income and assets are low enough, the individual will simultaneously qualify for and receive SSI.

c. Means-Tested Public Benefits

Means-tested benefits have eligibility criteria, and they include SSI, Medicaid, Medicare Saving Programs (sometimes called "Buy-In"), VA pension, subsidized housing, temporary assistance for needy families (TANF), prescription drug programs, and many various state public benefit programs such as SSI state supplement. This article briefly touches on the core programs, but it is imperative for an attorney drafting a special needs trust and for a trustee administering a trust to understand that eligibility rules for means-tested public benefits are not uniform between each federal and state agency.

In general, means-tested programs have a specific income limit and asset limit. They may also have other eligibility criteria in addition to those limits, such as age or disability requirements. Some programs apply deeming rules, meaning the income and assets of others in the household are considered. Many means-tested public benefits impose a transfer penalty (usually a period of ineligibility) if the applicant has transferred his or her assets in a prescribed "look back period."

i. Supplemental Security Income (SSI)

SSI is a federal cash benefit program.[5] Individuals are eligible for SSI if they are age 65 or older, blind, or permanently and totally disabled.[6] The income limit to qualify for SSI is $733 per individual or $1,100 per couple. Income includes all earned and unearned income as well as "in-kind support and maintenance" (ISM). ISM is anything a person receives in cash or in-kind that can be used to meet a person's needs for food or shelter. For example, ISM would include the value of rent payments if a parent was paying for a disabled child's rent.

An individual must have no more than $2,000 in "countable" assets to qualify for SSI. Many assets are considered non-countable assets and are therefore excluded from the strict asset limit; these include the individual's primary residence, one vehicle, household goods and personal effects, burial plot and burial arrangements, etc.

In evaluating eligibility for SSI, the SSA considers the assets and income of the parents of a disabled minor child and a spouse living in the same household with the disabled individual. Again, this is known as "deeming." The SSI program also has a transfer-of-assets penalty for any assets disposed of within three years of applying for benefits or while receiving benefits. The penalty is a disqualification of the individual from receiving benefits for a period of time.

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[5] SSI rules can be found in the Social Security Program Operations Manual (POMS).

[6] 42 U.S.C. § 1382c(a)(1)(A), the Social Security Administration applies the same disability standard as discussed above in Section 2.

The penalty period is determined by dividing the value of the asset disposed of by the federal benefit rate, currently $733.

It can be difficult to discern whether a client is receiving SSI or SSDI, and often the client is unaware which they receive. Requesting this information directly from the SSA will prevent any misunderstandings and ensure accurate facts.

ii. Medicaid

Medicaid is a health benefit program funded by both federal and state governments. Each state has its own statutes and regulations to administer its Medicaid program. Different states may apply different names: MassHealth in Massachusetts, MaineCare in Maine, and Medi-Cal in California.

The federal government has required states participating in the Medicaid program to provide health care needs to certain groups of individuals including eligible elderly age 65 and older, adults and children with disabilities, pregnant women, and low income children and families.

Many states base Medicaid eligibility on SSI eligibility such that an individual who receives SSI benefits is automatically eligible to receive Medicaid, while other states use different eligibility criteria. For specific income and asset limits, as well as any applicable transfer-of-asset penalty, consider the Medicaid agency's manual or guide for the state from which the beneficiary receives benefits or is likely to receive benefits.

iii. VA Benefits

VA benefits that are means-tested include pension, housebound, and aid and attendance. In order to receive these VA benefits, a veteran must: have served at least 90 days, one day of which was during a period of war, must have a discharge that is less than dishonorable, and must be permanently disabled or age 65 or older. If the veteran meets these requirements, he or she will be eligible for the benefit if he or she also meets the financial eligibility criteria.

Currently, these are not strict limits like with SSI. For income, the total household income reduced by any unreimbursed medical expenses cannot exceed the maximum allowable pension rate for the veteran. It is generally understood that the countable assets for the applicant must total $80,000 or less but this is not in writing, and currently there is no definitive asset limit.

Early in 2015, the Department of Veterans Affairs proposed changes to the VA pension rules. There was a period for public comment, and we wait for final regulations to be issued. If adopted, the proposed changes would be sweeping and would include a definitive limit on net worth, the treatment of income as an asset, a lookback period and a transfer penalty.

Be cautious about relying on a special needs trust to qualify an individual for VA benefits. One decision of the VA General Counsel held that assets in a special needs trust "while maximizing the use of governmental resources in the care and maintenance of the claimant, should be considered in calculating the claimant's net worth for improved-pension purposes" VAOPGCPREC 33-97.

iv. Housing Assistance

The relationship of special needs trusts and public housing benefits is complicated. When advising an individual regarding the creation and administration of a special needs trust, it is essential that the drafting attorney or trustee be aware of the eligibility rules for the specific housing benefit. The attorney or trustee should also be aware whether there are income or asset limits and whether transfers by the individual will result in imputed income.

The U.S. Department of Housing and Urban Development (HUD) administers most (but not all) of the available assisted housing programs. At the moment and in general, there is no asset limit. Income eligibility requires an individual's countable income to be less than 80% of the median income of the area to be considered "low income," less than 50% to be considered "very low income," and less than 30% to be considered "extremely low income." Income for subsidized housing purposes includes earned and unearned income, SSI, SSDI, pension, unemployment, alimony, child support, and any interest generated by assets if family assets are over $5,000 in value.

However, the Housing Opportunity Through Modernization Act of 2016 became law at the end of July of 2016. Here are some of its features:

- The Act prohibits public housing assistance to families that have "net family assets exceeding $100,000 annually (adjusted for an inflation) or an ownership interest in property that is suitable for occupancy." There are several exclusions, particularly for the value of any retirement account.
- Even for those already living in public housing, there is a new income limit. If the tenant's income exceeds 120% of the area median income for two consecutive years, the HA must either evict the tenant, charge FMV rent, or charge the government's cost to maintain the unit.
- Section 104 is titled *Limitation on Eligibility for Assistance Based on Assets* and specifically 104(2)(C) addresses trust funds: "In cases in which a trust fund has been established and the trust is not revocable by, or under the control of, any member of the family or household, the value of the trust fund shall not be considered an asset of a family if the fund continues to be held in trust. Any income distributed from the trust fund shall be considered income for purposes of section 3(b) and any calculations of annual family income, except in the case of medical expenses for a minor."

The U.S. Department of Housing and Urban Development is now tasked with creating regulations, and these may provide more guidance.

4. Would a Special Needs Trust Be Useful If the Beneficiary Is Not Receiving Means-Tested Public Benefits?

If the objective is for an individual to retain eligibility for means-tested public benefits, a special needs trust may be appropriate if none of the alternatives discussed in Section 5 are appropriate. The trust is designed to hold the assets in a way that they can be used for the benefit of the beneficiary without being counted as available resources to the beneficiary. The

trust can be used as a proactive rather than a reactive planning tool. If an individual meets the SSA standard for a disability but is not currently receiving means-tested public benefits, his or her assets may be transferred to a first party special needs trust to establish eligibility. For a third party trust, a convertible trust may be appropriate as discussed in Section 9.

If the individual does not and will not receive means-tested public benefits, another type of trust may be appropriate (e.g. a spendthrift trust for a beneficiary who might otherwise mismanage assets), but it would not be a special needs trust.

5. Are There Alternatives to Special Needs Trusts?

Even when an individual is dependent on means-tested public benefits like SSI or MaineCare, a special needs trust may not be necessary even if the individual receives or is entitled to receive assets that would increase assets above the relevant limits. There may be other appropriate tools to protect those benefits or it may be appropriate to forego the benefits for a period of time.

a. Spend-Down

If the windfall received is relatively modest or the individual has current needs, consider spending down the amount rather than a special needs trust. The individual with disabilities will want to spend down his or her assets to less than the maximum allowable assets for the particular public benefit program. If the spend-down occurs by the end of the month, his or her benefits should not be disrupted.

If funds are anticipated, try to time receipt for the very beginning of the month. This provides more time to accomplish the spend-down. Urge the individual to have a plan for spend-down (or "wish list") in place before the receipt of funds so that the spend-down can be promptly accomplished.

Funds must be spent for the exclusive benefit of the individual to avoid a transfer penalty. However, the funds can be spent on almost any goods and services for the individual. Some examples of appropriate spend-down purchases include: buying a home or paying off a mortgage on a home; paying rent for that calendar month only or possibly paying rent for a year in advance; home repairs; real estate taxes paid in advance; buying home furnishings, appliances, and bedding; buying a computer, television, or game system; purchasing entertainment, including magazines, movie and concert tickets, and sporting events; paying off debts; pre-paying burial arrangements; paying medical expenses and bills not covered by Medicaid or Medicare (e.g., better quality wheelchair) and purchasing experimental drugs and alternative therapies; paying for dental expenses, eye glasses, physical therapy, and support services not covered by public benefits; and paying professionals like an attorney for estate planning and public benefits planning.

The individual should be sure to keep receipts in case proof is required by the government agency at the end of the month when the spend-down is complete and accounts are back to being below the required asset limit.

b. Transfer of Assets

In some cases, excess resources can be transferred to third parties to preserve eligibility for public benefits, but proceed with caution. As discussed above, there is an SSI transfer penalty, which is calculated by dividing the value of the transfer by the maximum SSI payment, currently $733. For example, a transfer of only $20,000 by an SSI recipient results in a 27-month period of ineligibility for SSI and the possible forfeiture of the SSI-linked Medicaid. But if the individual is receiving only Medicaid, not SSI, transferring assets may not have a negative effect on benefits.

c. ABLE Accounts

The Achieving a Better Life Experience Act (ABLE Act) was passed by Congress in 2014 and allows states to set up programs that permit individuals with disabilities or their family members to make contributions to 529A accounts, similar to 529 education accounts. The ABLE account is a tax-preferred savings account that does not jeopardize the beneficiary's eligibility for means-tested public benefits.[7] Currently ABLE accounts have been established in Ohio, Tennessee, and Nebraska but these accounts are all open-enrollment for all state residents.

Funds in ABLE accounts of up to $100,000 will not affect an individual's eligibility for SSI. Funds of more than $235,000 or $452,210 (depending on the state) will not be counted for the purpose of Medicaid eligibility. This gives the beneficiary an opportunity to save money and pay for additional needs themselves, without being disqualified from the means-tested public benefits that provide for their basic support.

These accounts are ideal for individuals with disabilities who have a small amount of money over the asset eligibility requirement for public benefits. An ABLE account can avoid a spend-down of assets and the expensive costs of creating a special needs trust.[8] An ABLE account is also a good option if the individual or family would like the beneficiary to have more control over his or her own assets.

But ABLE accounts do have limited applicability and usefulness. In order to meet the criteria for an ABLE account, the beneficiary's disability must have been established before age 26. An individual can only have one ABLE account, but the individual, family members, and others may all contribute to that one account. However, there is a maximum contribution

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[7] For additional information on ABLE accounts and how they compare to special needs trusts, the reader is encouraged to consider the materials on California Attorney Stephen Dale's *Achieving Independence* website as well as the article *A Comparison of 529 ABLE Accounts, Pooled Special Needs Trusts, and Special Needs Trusts*, written by Joanne Marcus and Theresa Varnet and published by NAELA. (http://naela.informz.net/NAELA/data/images/PDFs/SpecialNeedsPlanningArticle-MarcusVarnetFINAL.pdf. MarcusVarnetFINAL.pdf.)

[8] There may be fees for ABLE accounts as well, but these costs are minimal compared to creating and administering a special needs trust. For example, the ABLE account program in Ohio, known as STABLE accounts, has a free account set-up with a $5.00 per month fee and an asset-based fee. http://www.stableaccount.com/

amount per year. It is set at the federal gift tax exclusion which is currently $14,000 in a single year.

While the beneficiary does have more control over distributions from an ABLE account than a special needs trust, there is a tax imposed on distributions if those funds are not used for "qualified disability expenses." Fortunately, the qualified expenses include most purchases made to improve the health, independence and quality of life of the beneficiary. Examples of non-taxable expenses include education, transportation, healthcare expenses, and household costs.

Finally, ABLE accounts must include a Medicaid payback provision. Upon the death of the beneficiary, the remaining account balance—regardless of whether those funds were contributed by the individual, were gifts from family, or were earnings within the account—must be paid to the state Medicaid agency to reimburse it for medical costs. Only after this payback would any funds be distributed to family members or other beneficiaries.

6. What Are the Differences Between a First Party Special Needs Trust and a Third Party Special Needs Trust?

Once it is determined that a special needs trust is appropriate, the next question is which type of special needs trust should be used. There are several types of special needs trust, and a comparison of some of those is included in Appendix C. Although special needs trusts can be distinguished from one another in many ways, the most important distinction is between first and third party trusts. These two types of trusts are treated differently for tax purposes, benefit determinations, and payback requirements.

a. First Party Special Needs Trusts

The easiest way to differentiate between a first party and a third party special needs trust is by asking "Whose assets are to be transferred into the trust?" A first party trust is funded with assets that belong to the individual for whom the trust is being created and who is the intended beneficiary. Since these trusts are funded with assets that belonged to that individual, they are often referred to as *self-settled special needs trust*s.[9]

A first party special needs trust should be considered when an individual with disabilities owns or acquires assets and wants to become or remain eligible for means-tested public benefits. The need for a first party special needs trust typically arises when the individual receives a personal injury settlement, an inheritance, or a gift. Individuals who are otherwise eligible for means-tested public benefits remain eligible despite the availability of their assets (at the trustee's discretion) in the first party special needs trust, so long as the trust meets the statutory criteria set forth in OBRA 93.

OBRA 93 provides the following requirements for a valid first party special needs trust:

[9] Other names include *d4A trusts* which refers to the section of the Omnibus Budget Reconciliation Act (OBRA) of 1993 in which Congress recognized and codified this type of self-settled special needs trust; *payback trusts* or *under-65 trusts*, both names reference the statutory requirements imposed by 42 U.S.C. § 1396p(d)(4)(A).

- The trust must be funded with the assets of the individual who will be the sole beneficiary of the trust during his or her lifetime.
- The trust beneficiary must be under age 65 when the trust is established. Assets in the trust will remain exempt for the purpose of Medicaid eligibility after age 65, but any assets transferred into the trust after age 65 will be countable.
- The trust beneficiary must be disabled as defined by the Social Security Act in 42 U.S.C. § 1382c(a)(3). If the individual is not already receiving SSI or Medicaid, the disability will have to be confirmed by the Disability Determination Service.
- The trust must be "established" pursuant to a court order or by a parent, grandparent, or guardian of the beneficiary. Currently, a d4A trust may not be established by the beneficiary, which results in one of the oddities of d4A trusts.[10] Although the beneficiary is the "grantor" or "settlor" of the trust as his or her assets will fund the trust, the beneficiary cannot sign the trust document and cannot fund the trust directly.
- The trust must include a payback provision which provides that state Medicaid agencies will receive all amounts remaining in the trust upon the death of the beneficiary up to the amount of medical assistance paid since birth, not just since the event creating the disability or since creation of the trust. Only two categories of expenses have priority to the Medicaid payback: state or federal taxes due because of inclusion of the trust in the beneficiary's estate, and reasonable fees for administration of the trust estate. If more than one state has provided benefits, the amount available will be prorated. If there are any trust assets remaining, other expenses of the trust may be paid (e.g., funeral expenses, debts owed to third parties) and then the balance may be distributed to remaindermen.

When a first party special needs trust is established and administered correctly, the transferring of assets into the trust does not create a transfer-of-assets penalty, nor do the trust assets get counted as available resources for means-tested public benefit purposes.

b. Third-Party Special Needs Trusts

A third party special needs trust is less complicated than a first party special needs trust. Third party trusts are funded with the assets of someone other than the trust beneficiary. This donor, called the "grantor" or "settlor," wants to provide for an individual with disabilities without jeopardizing that individual's eligibility for means-tested public benefits. Typically this will be a parent or grandparent that wants to establish the trust for a disabled child or grandchild.

A third party trust can be created in two different ways: by will, known as a testamentary third party special needs trust, or during the grantor's life, known as a "freestanding" or "living" third party special needs trust. A testamentary third party trust must be used in the context of Medicaid planning when a community spouse (typically the healthier spouse) intends to preserve assets from the long-term care expenses of the other spouse in the event that the

[10] The Special Needs Fairness Act seeks to enable competent individuals to establish their own special needs trusts. It was passed unanimously by the Senate on September 9, 2015. The National Academy of Elder Law Attorney's Public Policy Manager tracks progress on the Special Needs Trust Fairness Act of 2015 (H.R. 670/S. 349) at https://www.naela.org/Public/Advocacy_Public_Policy/Public_Policy/SNT_Fairness_Act.aspx.

community spouse dies first. The will provides that all or a portion of the deceased spouse's assets will be held in the testamentary trust for the lifetime of the surviving spouse and be used to supplement and not supplant public benefits, subject to the discretion of the trustee. Upon the death of the surviving spouse, the remaining trust assets will be distributed as the community spouse provided in his or her will, typically to the couple's descendants.

A freestanding third party special needs trust on the other hand, can be funded during life by the grantor and by others. Because the trust comes into existence at the time it is created, the grantor can see that the trust is being administered as he or she wished. Another benefit is that the trust agreement can be amended, as appropriate, to comply with changes in the law.

There are few rules governing third party special needs trusts because the beneficiary never owns or controls the assets that become part of the trust. It is important that the trust terms not create any entitlement for the beneficiary to either the income from or the principal contained in the trust, and that the trustee has complete discretion over distributions to the beneficiary. If the trust reflects those provisions, the assets in the third party special needs trust will not be considered available resources to the beneficiary for means-tested public benefit eligibility purposes.

The key differences of third party special needs trusts from first party special needs trusts are as follows:

- A third party special needs trust will never be a "self-settled" trust and should never accept any assets of the beneficiary. In doing so, the trust is deemed to be "polluted" and the trust assets become countable, thereby disqualifying the beneficiary from means-tested public benefits.
- There is no "payback" provision. That is, there is no requirement that trust assets remaining in a third party special needs trust after the beneficiary's death be reimbursed to states that provided medical assistance to the beneficiary.
- A third party special needs trust can be drafted to benefit more than one beneficiary.
- The grantor gets to hand-pick the trustee and successor trustees, highlight the objectives of the trust, and decide how any remaining assets of the trust are to be distributed upon the death of the beneficiary.

A third party special needs trust is often considered in the context of estate planning by the parent, grandparent, or other person who wants to provide for the individual with disabilities. For example, suppose a parent died intestate or prepared a simple will with no planning for her child with disabilities who is dependent on SSI and Medicaid. The parent's assets will be distributed outright to the child who will then lose eligibility. It is possible that one of the alternatives to a special needs trust, described in Section 5, will be appropriate. If not, then to protect the child's future public benefits, a first party trust with a payback provision will be necessary. This is a reaction to the circumstances, not proactive planning. Instead, if the parent had planned for creation of a third party special needs trust, either freestanding or testamentary, the trust would receive the assets, protect eligibility for means-tested public benefits, and not need to include a Medicaid payback provision.

7. What is the Difference Between a d4A Special Needs Trust and a d4c Pooled Special Needs Trust?

A d4A special needs trust is another name for an individual first party special needs trust. A d4A trust is created for the sole benefit of an individual with disabilities who is under age 65 and (at the moment) must be established by the individual's parent, grandparent, guardian, or a court.

A d4C special needs trust is a pooled trust created and administered by a nonprofit organization. A pooled trust holds the resources of many beneficiaries, but each beneficiary's assets are maintained in a separate account. A pooled trust may be created by the individual or by the individual's parent, grandparent, guardian, or a court, and, in some cases, may be established for someone over the age of 65. Upon the beneficiary's death, the remaining funds in the pooled trust either remain in the pooled trust for the other beneficiaries or are used to payback Medicaid benefits the beneficiary received. Additionally, the trustee of a pooled trust cannot be changed.

Pooled trusts are a good option if there are limited means to create a special needs trust. Because a pooled trust is already established, joining the already formed trust is a cheaper route. These trusts may also be an option if there is no trustee available to administer the first party special needs trust for the beneficiary.

Note: There are also pooled trusts for third party funds.

8. What is a Sole Benefit Trust?

First party and third party special needs trusts are the two primary types of special needs trusts used to preserve the eligibility for means-tested public benefits for the intended beneficiary. However, a sole benefit trust can be appropriate in certain circumstances.

A sole benefit trust considers the eligibility for public benefits for both the grantor and the beneficiary. Sole benefit trusts are often used when an older parent of a child with disabilities needs long-term care that could be paid for with Medicaid benefits. Unlimited assets may be transferred from the parent to a properly drafted sole benefit trust for the benefit of a child with disabilities. The state Medicaid agency will not impose a Medicaid transfer penalty on the parent whose assets were transferred, and the establishment of the trust will not disqualify the beneficiary from means-tested public benefits.[11] For the transfer to not result in a transfer

[11] The statutory authority for sole benefit trusts is OBRA 93, codified at 42 U.S.C. § 1396p(c)(2)(B). It exempts from the Medicaid transfer penalty assets that:

> (i) were transferred to the individual's spouse or to another for the sole benefit of the individual's spouse,
> (ii) were transferred from the individual's spouse to another for the sole benefit of the individual's spouse,
> (iii) were transferred to, or to a trust (including a trust described in subsection (d)(4) of this section) established solely for the benefit of, the individual's child described in subparagraph (A)(ii)(II); or

penalty for the grantor, the trust must satisfy the "solely for the benefit of" the beneficiary requirement, which is interpreted by the SSA similar to a first party trust.

States have varying interpretations of sole benefit trust criteria, so it is essential that the drafter be aware of the idiosyncrasies in the relevant state. For example, the Maine Department of Health and Human Services takes the position that a sole benefit trust must either include payback provisions or be "actuarially sound."

9. What is a Convertible Trust?

A convertible trust is another form of third party trust. This would be used when a client wants to provide for a loved one but the client is not sure whether that loved one will be dependent on means-tested public benefits in the future. In that case, the estate planning vehicle (whether by will or freestanding trust) may begin as a support trust that is flexible enough to convert to a discretionary special needs trust in the future.

The purpose of a convertible trust is to retain the right to "convert" the trust to a special needs trust. In most cases, a convertible trust might be considered where the beneficiary's disability determination has not yet been secured.

10. How is a Special Needs Trust Administered?

The trustee of a special needs trust, whether a first party, third party, or sole benefit trust, has sole, absolute, and unfettered discretion regarding distributions and purchases from the trust corpus. When called upon to make a particular distribution or purchase, a trustee should always look to the language of the trust agreement, be familiar with the laws governing the trust, and be aware of the changing public benefit rules and the impact on the trust beneficiary when making that distribution or purchase.

For example, when the beneficiary of a special needs trust is receiving SSI benefits, the trustee must understand the negative impact on those benefits of paying for food or shelter from the trust and of distributing cash to the beneficiary. The trustee can provide many other goods and services for the beneficiary such as physical therapy, medical treatment, medications, education, entertainment, travel, some utilities (like cable television and a telephone), household furniture, taxes, and legal fees, without affecting benefits.

A special needs trustee must keep abreast of the SSA's and state Medicaid agency's changing interpretations and treatment of special needs trusts. In March of 2005, the old prohibition against providing clothing was dropped by the federal government, so the trustee may now make clothing purchases and it will not affect the benefit amount or eligibility of the

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(iv) were transferred to a trust (including a trust described in subsection (d)(4) of this section) established solely for the benefit of an individual under 65 years of age who is disabled (as defined in section 1382c(a)(3) of this title).

beneficiary. In May of 2012, the SSA took the position that the trustee can only pay for travel expenditures of a caregiver family member if that family member has been medically trained.

Administering a special needs trust is generally more challenging than drafting the trust agreement and establishing the trust.

Conclusion

This article is intended as a mere introduction to special needs trusts and their alternatives. A summary of some of the decisions to be made as discussed in this article appear in the decision tree attached as Appendix D. A worksheet for assessing the suitability of a special needs trust is offered at Appendix E.

The reader is strongly encouraged to consult other resources, to mentor with experienced practitioners, and to stay current with changes by federal and state agencies. A special needs trust is intended to improve the quality of life for an individual with disabilities, but the wrong type of special needs trust for a particular situation or faulty administration of the trust can disqualify the beneficiary from much-needed, means-tested public benefits and disrupt his or her network of support.