

TIME TO TERMINATE

*2020 Stetson University National Conference on Special Needs Planning and
Special Needs Trusts*

Presented By:

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TIME TO TERMINATE

Trusts can be terminated for myriad reasons. A revocable trust may be revoked. A revocable or irrevocable trust may expire in accordance with the terms of the trust. There may no longer be a good reason for the trust to continue. The trust may be uneconomical to administer. Sometimes, circumstances may warrant decanting the assets into a new trust.

Generally, the death of a beneficiary will trigger the termination of a first party (self-settled) or third party special needs trust. There are circumstances, however, that sometimes warrant the termination of a special needs trust during the beneficiary's lifetime. For example, the beneficiary may no longer meet the disability criteria for receiving means-tested public benefits such as Supplemental Security Income (SSI) or Medicaid, or may not want to receive means-tested public benefits any longer, or the assets held in the special needs trust may not be sufficient to justify the costs of administering the trust. The process of terminating the trust will depend on the terms of the trust, the type of trust and federal and state law.

Terminating a Self-Settled Special Needs Trust Upon the Death of the Beneficiary

Medicaid Payback

Medicaid and SSI rules require a self-settled special needs trust to contain a provision that upon the death of the beneficiary, any state agency that has provided Medicaid benefits must be repaid out of the trust up to the amount of the benefits provided during the existence of the trust. *See* 42 *U.S.C.* §§ 1396p(d)(4)(A), 1382b(e)(5) and 1382b(c)(1)(C)(ii). The states must have priority over the payment of debts and administrative expenses other than those set forth in POMS SI 01120.203E.

There has been some confusion among practitioners and professionals who deal with self-settled special needs trusts regarding the extent of the Medicaid payback. In particular, there has been some debate as to whether the Medicaid lien encompasses procurement costs and reductions pursuant to *Ark. HHS v. Ahlborn*, 547 U.S. 268 (2006)¹ when the trust has been funded with the proceeds of personal injury settlements or court awards. Some practitioners also erroneously believe that the payback is limited to Medicaid payments made after the establishment of the special needs trust. The Social Security Program Operations Manual System (POMS) states that the Medicaid agency must be reimbursed for medical assistance paid prior to the establishment of the special needs trust as well as for medical assistance paid on behalf of the beneficiary during the administration of the special needs trust. POMS SI 00120.203B (“Medicaid payback ... cannot be limited to any particular period of time; for example, payback cannot be limited to the period after establishment of the trust”).

The payback also cannot be limited to any particular state. *Id.* If there are not enough funds in the trust to reimburse each state that provided Medical assistance to the beneficiary, the trustee must reimburse each state on a *pro rata* basis. In wrapping up the trust, the trustee must obtain statements from each state that provided medical assistance to the beneficiary setting forth the amount of the payback to determine how much each state will be paid.

Trustees should carefully scrutinize the statements received from the Medicaid agencies as they may contain errors. Although errors can be challenged, trustees should consider whether it’s worth the time, effort and cost to mount such a challenge. Additionally, trustees should be

¹ The *Ahlborn* ruling was codified in Section 53102 of the Bipartisan Budget Act of 2018. The Medicaid lien is limited to medical expenses and does not include damages for pain and suffering or future lost wages.

aware that capitation fees are subject to Medicaid payback.² Such a fee will be imposed in a state using the capitation model if the beneficiary was receiving SSI benefits in a state where the SSI recipient automatically receives Medicaid even if the beneficiary never actually accesses the Medicaid benefits.

Allowable Expenses

Although the special needs trust ends when the beneficiary dies, the trustee is authorized to take steps to conclude the trust administration in addition to distributing the trust assets to the remainder beneficiaries. Certain taxes may be paid from a self-settled trust prior to paying back the Medicaid agency, assuming the trust document authorizes such expenditures. These include federal and/or state taxes that are due from the trust because of the death of the trust beneficiary. In addition, the trust can also provide for the payment of reasonable fees for the trust administration, including trust accountings submitted to a court and the completion and filing of documents, such as tax returns, or other actions that are required to terminate and wrap up the trust. *Id.*

Prohibited Expenses

Generally, the payment of funeral expenses prior to Medicaid reimbursement is prohibited. For this reason, trustees should consider the funding of an irrevocable burial trust while the beneficiary is still alive. If funds will remain in the trust after the agency is paid back, the trustee may be permitted to pay for a funeral absent language in the trust prohibiting such payment.

² Medicaid managed care provides for the delivery of Medicaid health benefits and additional services through contractual arrangements between the state Medicaid agencies and managed care organizations (MCOs) that accept a set amount per member per month payment for those services. That set amount is the capitation fee.

Trustees are also prohibited from paying certain taxes prior to paying the Medicaid lien. These include estate taxes other than those stemming from the inclusion of the special needs trust in the beneficiary's estate and inheritance taxes that may be imposed for remainder beneficiaries. *Id.*

The Medicaid lien must be paid before payments of debts to third parties are made. Additionally, payments to residuary beneficiaries cannot be made until the Medicaid lien is paid. *Id.* Trustees may be personally liable for improper distributions so they should proceed with caution.

Early Termination of Self-Settled Special Needs Trusts

Recognizing that the beneficiary may no longer be disabled, or otherwise may be ineligible for SSI or Medicaid, or the trust may be uneconomical to administer, the Social Security Administration revised its POMS in 2010 to provide three requirements for early termination provisions in self-settled special needs trusts. SI 01120.199. First, upon terminating the trust prior to the beneficiary's death, the state must be paid back all amounts remaining in the trust at the time of termination up to an amount equal to the total amount of medical assistance paid on behalf of the beneficiary. Second, other than payments for expenses set forth in SI 01120.199F3 and SI 01120.201F.4, all funds remaining in the trust after payback must be distributed to the trust beneficiary. These permissible expenses including Federal and state taxes due as a result of the trust termination and reasonable fees and administrative expenses related to the trust. Third, the beneficiary cannot have the power to terminate the trust.

Previously approved trusts that contain defective early termination provisions can be amended to conform to the requirements of SI 01120.199 within 90 days. The 90 day period begins to run on the date that the beneficiary or representative payee for the beneficiary is

informed that the trust provisions must be amended. SI 01120.199A.2. The Social Security Administration permits only one 90-day period to amend the early termination provisions of the trust. *Id.*

Terminating Third-Party Special Needs Trusts Upon the Death of the Beneficiary

Third-party special needs trusts are not subject to Medicaid payback requirements. Therefore, the trustee should pay any debts, file tax returns and pay taxes, pay administrative fees and then distribute the balance of the assets in accordance with the terms of the trust. The trust document may provide that upon termination the trust may pay funeral expenses and estate taxes unrelated to the trust.

A third-party special needs trust usually will contain spendthrift provisions to insulate the trust funds from claims of creditors of the trust beneficiary. The trust, however, may contain language permitting such payments. The trustee should pay trust debts before paying personal debts of the beneficiary if the funds remaining in the trust are insufficient to pay both.

How to Terminate Special Needs Trusts Before the Death of the Beneficiary

The withdrawal of trust property does not terminate the trust. The trust continues to exist even though the trustee may no longer have any duties to perform in administering the trust. Steps must be taken to actually terminate the trust.

The trust document may contain the procedure for terminating the trust. For example, a self-settled special needs trust may specify that court approval is required. A third-party trust may provide that the trust can be terminated if it contains less than a certain amount of assets. Accordingly, the trust document must be reviewed when early termination is contemplated to ascertain whether it provides for the manner in which the trust can be terminated.

In the absence of provisions in the trust addressing the method of termination, the Uniform Trust Code (“UTC”) may govern such terminations.³ As states may have revised the language of certain UTC provisions, trustees should follow the code provisions adopted by the states governing the trust.⁴ Where the situs of the trust is in a state that has not adopted the UTC, the trustee must review the law governing terminations in that state.

The UTC provides that noncharitable irrevocable trusts can be terminated upon consent of the grantor and all beneficiaries, even if the termination is inconsistent with a material purpose of the trust. UTC § 411. The grantor’s power to consent to termination may be exercised by an attorney-in-fact for the grantor only to the extent that such authorization is expressed in the power of attorney document or in the trust. A grantor’s conservator or guardian may also consent to a trust termination with approval of the court supervising the conservatorship or guardianship. *Id.* While some states have adopted this provision without modifications, some states have adopted different versions of this provision. For example, New Jersey’s version specifies that a trust may be terminated upon consent of the trustee and all beneficiaries, if the termination is not inconsistent with a material purpose of the trust. N.J.S.A. 3B:31-27.

The UTC provides that a trustee or beneficiary may commence a court proceeding to approve or disapprove a proposed trust termination. UTC § 410(b). A court may terminate a noncharitable irrevocable trust upon consent of all of the beneficiaries if the court concludes that the continuance of the trust is not required to achieve any material purpose of the trust. UTC § 411(b). A spendthrift provision in the trust is not presumed to constitute a material purpose of the trust. UTC §411(c). If not all of the beneficiaries consent to the termination, the court

³ To date, 34 states and the District of Columbia have adopted a version of the UTC.

⁴ As this paper is addressed to a national audience, references generally will be made to provisions of the Uniform Trust Code.

nevertheless may approve the termination if it is satisfied that 1) the trust could have been modified if all of the beneficiaries had consented and 2) the interests of the beneficiary who does not consent will be adequately protected.

The UTC permits the court to terminate a trust over a trustee's objection; however, the trustee has standing to object to the proposed termination pursuant to UTC § 410. Article 3 of the UTC on representation, virtual representation and the appointment and approval of court-appointed representatives apply to the determination of those who can consent on behalf of a beneficiary.

Under the UTC, a court may terminate a trust if, because of circumstances not anticipated by the grantor, termination will further the purposes of the trust. UTC § 412. Upon termination under this section, the trustee must distribute the trust assets in a manner consistent with the purposes of the trust. *Id.*

The UTC also permit a court to terminate an uneconomic trust. A trust containing a total value of \$50,000 or less may be terminated upon notice to the qualified beneficiaries⁵ if the trustee concludes that the value of the trust assets is insufficient to justify the administration expenses. UTC § 4.14. This amount, however, may differ by state. For example, New Jersey's version of the UTC permits the court to terminate trusts having a total value less than \$100,000. N.J.S.A. 3B:31-30.a. Pennsylvania's version, on the other hand, does not specify a dollar amount. 20 Pa.C.S. § 7740.4(a).

The UTC provides that upon termination of the trust, the trustee may send the beneficiaries a proposal for distribution. UTC § 817. "The right of any beneficiary to object to the proposed distribution terminates if the beneficiary does not notify the trustee of an objection

⁵ The term "Qualified Beneficiaries" is defined in UTC § 103(13).

within 30 days after the proposal was sent but only if the proposal informed the beneficiary of the right to object and of the time allowed for the objection.” *Id.*

The trustee may want to provide a final accounting to the beneficiaries, or the beneficiaries may agree to waive their right to an accounting. The trustee should obtain a written consent to the accounting or a written waiver of the accounting before distributing the assets to the remainder beneficiaries.

**SAMPLE TERMINATION OF TRUST WAIVER OF ACCOUNTING,
INDEMNIFICATION, REFUNDING BOND AND RELEASE OF TRUSTEE**

SCHENCK, PRICE, SMITH & KING, LLP
PO Box 991, 220 Park Avenue
Florham Park, New Jersey 07932-0991
(973) 539-1000

In the Matter of the

**THE SUPPLEMENTAL BENEFITS
TRUST FOR ***U/W/O ***DATED *****

**TERMINATION OF TRUST, WAIVER OF
ACCOUNTING, INDEMNIFICATION,
REFUNDING BOND AND RELEASE OF
THE TRUSTEE FOR THE PERIOD ***
THROUGH ***, 2020**

KNOW ALL PERSONS BY THESE PRESENTS THAT:

WHEREAS, *** (hereinafter "Decedent") died on ***, a resident of Morris County, State of New Jersey; and

WHEREAS, Decedent died testate, leaving a Last Will and Testament dated ***, 2010, (hereinafter "Will"); and

WHEREAS, Decedent's Will was admitted to probate by the Morris County Surrogate on ***, 2014; and

WHEREAS, pursuant to Article 4.1 of Decedent's Will the Decedent's residuary estate passes in equal shares to Decedent's sons, *** and *** ; and

WHEREAS, pursuant to Article 4.2 of Decedent's Will any share for **** passes into a Supplemental Benefits Trust for his benefit to be administered pursuant to the terms under Article 4.2 of Decedent's Will (hereinafter the "Trust"); and

WHEREAS, on ***, 2014 , *** was issued Letters of Trusteeship by the Morris County Surrogate thereby appointing him as trustee of the Trust; and

WHEREAS, on August 18, 2017 the Decedent's estate distributed \$93,729.27 into the Trust in full satisfaction of the amount the Trust was owed under the terms of Decedent's Will; and

WHEREAS, pursuant to Article 4.2(f) of Decedent's Will the Trust shall terminate upon the death of *** and the trustee shall distribute the balance of income and principal remaining in the Trust to the surviving issue of ***, or if none, to*** ; and

WHEREAS, ***died on May **, 2020, leaving no surviving issue; and

WHEREAS, as of July ***, 2020, the balance remaining in the Trust is EIGHTY ONE THOUSAND SIX HUNDRED THIRTEEN DOLLARS and FIFTY-THREE CENTS (\$81,613.53); and

WHEREAS, the Trustee now wishes to distribute the above balance of the Trust to *** (hereinafter the "Beneficiary"); and

WHEREAS, the Beneficiary has received notice from the Trustee that assets have been set aside in the approximate amount of EIGHTY ONE THOUSAND SIX HUNDRED THIRTEEN DOLLARS and FIFTY-THREE CENTS (\$81,613.53), to be paid, upon the Beneficiary signing and delivering to the Trustee this Termination of Trust, Waiver of Accounting, Indemnification, Refunding Bond and Release of Trustee (hereinafter the "Termination Agreement"); and

WHEREAS, the Beneficiary has expressed a preference to waive a formal accounting and that termination, settlement, and distribution be effected by agreement as herein provided in order to minimize delays and other inconveniences of judicial proceedings; and the Trustee is willing to consummate such settlement by means of, and in accordance with, this Termination Agreement.

IT IS THEREFORE AGREED AS FOLLOWS:

1. ***, hereinafter designated as the Obligor, is hereby held and firmly bound unto *** as Trustee of the Trust, hereinafter designated as the Obligee, having received a total distribution in the approximate amount of EIGHTY ONE THOUSAND SIX HUNDRED THIRTEEN DOLLARS and FIFTY-THREE CENTS (\$81,613.53), in full satisfaction of the distribution to which the Obligor is entitled pursuant to Article 4.2(f) of the Trust. All or a portion of this distribution shall be returned to the Obligee or to Obligee's Attorney, successors in office or assigns, to the extent that any part or the whole of the distribution shall at any time hereafter appear to be needed to discharge on behalf of the Trust any debt or debts, legacy or legacies, or additional unanticipated administrative expenses related to the Trust, for which the Obligee may not have other assets to pay, and that amount to be returned upon the Obligee's demand, shall be a pro-rata portion of said distribution or such part thereof as may be necessary for the payment of the said debt or debts, or additional unanticipated administrative expenses, or for the payment of a proportional part of the said legacies; and such debt or debts shall be deemed to include all taxes imposed upon or chargeable to the Trust, or owed by the Trust, including interest, penalties, costs, expenses and counsel fees, if any.

2. Approval of Administration. The Obligee has made available to the Obligor the books and records of the Trust for the period of administration from *** through ***, 2020, and through the date of the execution of this Termination Agreement (hereinafter sometimes referred

to as the "Book and Records"). The Obligor has been afforded the opportunity to audit the Books and Records through an independent auditor of his choosing, and does hereby ratify, approve and confirm all of the acts, transactions and proceedings of the Oblige in the administration of the Trust for the period from *** through ***, 2020, and through the date of execution of this Termination Agreement.

3. Representations. The Obligor does represent and warrant to the Oblige that he has not made any transfer or assignment or created any lien, mortgage or encumbrance upon or relating to the Trust or his respective rights or interests therein.

4. Final Distribution. The Oblige, upon the execution and delivery of this instrument, shall discharge any remaining obligations and shall distribute the assets remaining in the hands of the Oblige and payable to the Obligor, if any, including the net amount of any assets withheld from distribution to cover lagging expenses or any assets which shall subsequently be paid to the Trust; and the Obligor does hereby approve, ratify and confirm such distribution.

5. Indemnity. The Obligor, on behalf of the heirs, beneficiaries, successors and assigns of the Trust, agrees to indemnify and hold harmless the Oblige from any and all liability by reason of its acts, transactions and omissions, if any, in the administration of the Trust and in the investment, management and distribution of the Trust assets as reflected in the Books and Records from the date of inception of the Trust through the date of execution of this Termination Agreement, which may be asserted against the Oblige by anyone.

6. Release and Waiver of Accounting. The Obligor, by these presents, does remise, release and forever discharge the Oblige from all liabilities, claims and demands whatsoever, in law or in equity, on account of any acts, transactions or omissions, in respect to the Trust and to the Obligor's interests therein for the periods of administration above stated and through the date of the execution of this Termination Agreement; and the Obligor does further covenant and agree that he will not at any time request or demand any accounting whether in or out of court, or in any jurisdiction, relating in any way to the Trust for the period of administration above stated, and through the date of the execution of this Termination Agreement, or of any of the acts, transactions or proceedings of the Oblige in connection therewith.

7. Counterpart. This Agreement may be executed simultaneously or independently in one or more counterparts, each of which shall be deemed an original but all of which together shall constitute one and the same instrument.

IN WITNESS WHEREOF, this Termination Agreement has been signed and sealed by the Obligor and Oblige as of the date reflected on the Acknowledgment for each signature.

WITNESS

By: _____
*** , as Obligee

WITNESS

*** , as Obligor

ACKNOWLEDGEMENT

STATE OF NEW JERSEY)
 :
COUNTY OF) SS.:

BE IT REMEMBERED, that on _____, 2020, before me the subscriber, personally appeared *** , who I am satisfied, is the person named in and who executed the within Instrument, and thereupon did acknowledge that he signed, sealed and delivered the same as his act and deed, for the uses and purposes therein expressed.

Notary

STATE OF)
 :
COUNTY OF) SS.:

BE IT REMEMBERED, that on _____, 2020, before me the subscriber, personally appeared*** , who I am satisfied, is the person named in and who executed the within Instrument, and thereupon did acknowledge that he signed, sealed and delivered the same as his act and deed, for the uses and purposes therein expressed.

Notary

**SAMPLE ORDER TERMINATING SELF-SETTLED SPECIAL NEEDS TRUST
BEFORE DEATH**

SCHENCK, PRICE, SMITH & KING, LLP

220 Park Avenue

P.O. Box 991

Florham Park, New Jersey 07932

Attorneys for ***, Trustee

<p>,</p> <p>Plaintiff,</p> <p>v.</p> <p>Defendant.</p>	<p>SUPERIOR COURT OF NEW JERSEY</p> <p>CHANCERY DIV.:ESSEX COUNTY</p> <p>PROBATE PART</p> <p>DOCKET NO.:</p> <p style="text-align: center;"><u>Civil action</u></p> <p style="text-align: center;">ORDER</p>
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This matter having come before the court upon a motion by ***, Esq., attorney for ***, on notice to Schenck, Price, Smith & King, LLP, counsel for ***, Trustee of the *** Self-Settled Special Needs Trust (Shirley B. Whitenack, Esq., appearing), State of New Jersey, Office of the Attorney General on behalf of the New Jersey Division of Medical Assistance and Health Services (“DMAHS”) (***, DAG, appearing), and the Social Security Administration, seeking

