

Afterword: A Decade Later: Why Trustee Judgment Matters More Than Ever

Edward Wilcenski & Tara Anne Pleat

When the *Administration of Special Needs Trusts: Development of an Improved Approach* series was first published, it advanced a proposition that was not universally accepted: the administration of supplemental needs trusts should be governed first by traditional principles of fiduciary law—not by ad hoc judicial preferences or mechanical application of administrative guidance.¹ The articles argued that trustees should be evaluated under the familiar abuse-of-discretion standard applicable to discretionary trusts, supplemented only by those additional considerations unique to disability and public-benefit eligibility.²

At the time, that proposal represented a departure from prevailing practice. New York decisions frequently reflected inconsistent approaches, excessive reliance on agency personnel, and judicial substitution of a generalized "best interests" analysis for traditional fiduciary review.³ Trustees were left with little confidence regarding the standard by which their conduct would ultimately be judged. Two subsequent decisions—one from New York and one from the United States Supreme Court—suggest that the analytical framework proposed in the original article has aged well.

Matter of Ellen H.: Abuse of Discretion as the Organizing Principle

The most significant New York development came from *Matter of Ellen H. (Cassandra H.)*. Rather than evaluating every trust expenditure through the lens of whether it perfectly conformed to the Social Security Administration's Program Operations Manual System (POMS), the court framed its analysis as one of fiduciary discretion.⁴ The court expressly stated that it was applying an abuse-of-discretion standard and examined whether the trustee exercised reasoned judgment by considering three familiar questions: whether expenditures primarily benefited the beneficiary, whether governmental benefits were considered before

¹ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts*, N.Y. STATE BAR ASS'N J. 12, 19 (Mar. 2019); Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 22–24 (Mar. 2020).

² See Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts*, N.Y. STATE BAR ASS'N J. 12, 19 (Mar. 2019) (asserting that the abuse of discretion standard is the only standard that can effectively incorporate both the objectives of the benefit eligibility assessment and the best interest assessment); see also Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 22–24 (Mar. 2020) (stating that the abuse of discretion standard "provides the flexibility and protection afforded the trustees of other discretionary trusts so long as the trustee follows the commonly accepted rules of fiduciary conduct, as supplemented by additional steps that acknowledge the beneficiary's disability and eligibility for government benefits.").

³ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 24–25 (Mar. 2020) (discussing courts' reluctance to defer to trustee discretion and tendency to substitute judgment).

⁴ *Matter of Ellen H. (Cassandra H.)*, 82 Misc. 3d 1207(A), 2024 N.Y. Slip Op. 50248(U), at *3 (Sup. Ct. Broome Cnty. 2024).

trust assets were used, and whether the trustee reasonably concluded that trust funds nevertheless should be expended.⁵

Equally significant is what the decision did not do. The trustee was not surcharged because she failed to satisfy every administrative guideline. She was surcharged because she abandoned the fundamental obligations of fiduciary administration: maintaining adequate records, documenting decisions, avoiding self-dealing, accounting for trust assets, and demonstrating that expenditures were actually made for the beneficiary's benefit.⁶ The deficiencies identified by the court were failures of fiduciary process rather than mere failures of regulatory compliance. That reasoning closely parallels our proposed administrative protocol in *Administration of Special Needs Trusts: Development of an Improved Approach Part II*. The article argued that courts should protect trustees who engage in communication, investigation, consideration, and documentation—even if another trustee or judge might have reached a different substantive decision.⁷ Judicial review, we suggested, should focus on the quality of the fiduciary decision-making process rather than retrospective disagreement with the outcome.⁸

Loper Bright and the Proper Role of Administrative Guidance

Although *Loper Bright Enterprises v. Raimondo* arose outside the trust context,⁹ its implications for supplemental needs trust administration are difficult to ignore. By overruling *Chevron*,¹⁰ the Supreme Court rejected the notion that statutory ambiguity automatically requires judicial deference to an agency's interpretation.¹¹ Instead, courts must independently determine the best reading of the governing statute.¹² Thus, although POMS continues to serve an indispensable administrative function, explaining how the Social Security Administration administers SSI eligibility, it is not itself enacted law. After *Loper Bright*, courts are reminded that agency guidance informs legal analysis; it does not replace it. That principle mirrors the concern expressed in *Administration of Special Needs Trusts: Development of an Improved Approach* over the tendency of some courts to defer reflexively to public benefit administrators rather than independently applying trust law.¹³ The article questioned whether trustees should be judged primarily by

⁵ *Id.*

⁶ See *id.* at *17 (surcharging the Trustee after finding that she “failed to account properly or act in a prudent manner as fiduciary”).

⁷ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 22–24 (Mar. 2020).

⁸ *Id.*

⁹ See *Loper Bright Enters. v. Raimondo*, 603 U.S. 369 (2024) (bringing suit to challenge a rule implemented by the National Marine Fisheries Service).

¹⁰ *Id.* at 412.

¹¹ See *id.* at 413 (holding that “courts need not and under the APA may not defer to an agency interpretation of the law simply because a statute is ambiguous.”).

¹² *Id.* at 412.

¹³ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts*, N.Y. STATE BAR ASS'N J. 12, 16 (Mar. 2019).

administrative preferences or by established fiduciary principles.¹⁴ *Loper Bright* reinforces the latter approach by reaffirming that legal interpretation ultimately remains a judicial responsibility rather than an administrative one.¹⁵

A Convergence of Fiduciary and Administrative Law

Viewed together, *Ellen H.* and *Loper Bright* suggest that supplemental needs trust administration is moving toward a more coherent analytical framework. *Ellen H.* demonstrates that New York courts can evaluate trustees through traditional fiduciary principles while still recognizing the importance of public benefit rules. *Loper Bright* confirms that administrative guidance should be respected because it is persuasive—not because it automatically controls judicial interpretation. Neither decision diminishes the importance of POMS or Medicaid guidance. Rather, both decisions place those authorities in their proper role: valuable sources of expertise that inform, but do not displace, the trustee's fiduciary judgment or the court's independent legal analysis.

Conclusion

The central recommendation of *Administration of Special Needs Trusts: Development of an Improved Approach* was straightforward: supplemental needs trusts should be administered as discretionary trusts.¹⁶ Trustees should investigate, communicate, document, consider available public resources, and exercise reasoned judgment in light of the governing trust instrument and applicable law.¹⁷ Courts, in turn, should review those decisions under an abuse-of-discretion standard rather than substituting their own preferences or treating administrative guidance as controlling.¹⁸ A decade later, *Matter of Ellen H.* and *Loper Bright* point in the same direction. Together, they suggest that the law increasingly recognizes what we proposed all along—that the protection of beneficiaries and the protection of trustees are best achieved not through rigid adherence to agency guidance, but through faithful application of longstanding principles of fiduciary law.

¹⁴ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts*, N.Y. STATE BAR ASS'N J. 12, 19 (Mar. 2019); Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 22–24 (Mar. 2020).

¹⁵ See *Loper Bright Enters.* 603 U.S. at 403 (asserting that “Congress expects courts to do their ordinary job of interpreting statutes, with due respect for the views of the Executive Branch.”).

¹⁶ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts*, N.Y. STATE BAR ASS'N J. 12, 19 (Mar. 2019).

¹⁷ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 23–27 (Mar. 2020).

¹⁸ Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts*, N.Y. STATE BAR ASS'N J. 12, 19 (Mar. 2019); Edward V. Wilcenski & Tara Anne Pleat, *Administration of Special Needs Trusts Part II*, N.Y. STATE BAR ASS'N J. 22, 22–24 (Mar. 2020).

ADMINISTRATION OF SPECIAL NEEDS TRUSTS: DEVELOPMENT OF AN IMPROVED APPROACH

By Edward V. Wilcenski, Esq. and Tara Anne Pleat, Esq.¹

I. Introduction:

Most Elder Law and Special Needs Planning attorneys have developed a level of comfort with third party special needs trust practice. Many of the rules and concepts which apply to other trusts and which are used in a traditional estate planning practice carry over quite nicely.

The same cannot be said for the practice involving first party special needs trusts. Indeed, the very nature of first party trust practice defies efforts to create a uniform set of practice standards for drafting and administration.² By definition these trusts are funded with the property of individuals with disabilities (as opposed to parents or other benefactors), leading to practice variations based on:

- * disability, which can be cognitive, physical, or some combination of them;
- * the nature of the property interest, which can be the proceeds of a personal injury settlement, marital property, inherited or gifted assets, accumulated earnings, and federal and state benefits;
- * procedural context, which can be governed by the rules of the guardianship court if the trust is being funded in connection with a guardianship proceeding, the civil practice statute if the trust is being funded as part of a court approved litigation settlement, or the rules of the family court if the trust is being incorporated into a divorce proceeding; and
- * program rules for public benefits, including Supplemental Security Income, Medicaid and Section 8 among many others.

II. First Party Trust Administration: Uncertainty and Indecision

New York enacted a third party supplemental (special) needs trust (SNT) statute, Section 7-1.12 of New York's Estates Powers & Trusts Law (EPTL 7-1.12), in 1993. That same year Congress carved out an exception for first party trusts in the federal Medicaid

¹ The authors wish to express their thanks to NAELA Fellow Ron M. Landsman for his willingness to offer insight and comment on the ideas expressed in this article. His piece in the Spring 2014 issue of the NAELA Journal, cited in footnote 15, remains one of the most important writings in the area of special needs planning in many years.

² This article is based primarily on law and practice in New York State. While we have tried to focus on general concepts which we believe to be incorporated into special needs trust law and practice in other states, we are also aware that many states have modified these concepts by regulation and administrative rule.

program's transfer of asset penalty provisions,³ and in 1994 our state legislature amended EPTL 7-1.12 to be used as the drafting template for both types of special needs trusts.⁴ The result is something of a hybrid: a trust borne of federal Medicaid law governing asset transfers, framed within a state trust statute which codified the holding of a watershed state court decision on third party trusts.⁵

In New York, some courts – especially in the early years after the enactment of OBRA '93 – attempted to create drafting and administration standards for first party trusts.⁶

These early decisions are inherently fact- and forum-specific. They have led to as much confusion as clarity and offer little precedential value as trial court decisions. At best, they establish little pockets of common law applicable in similar proceedings involving cases with nearly identical facts.

A survey of New York case law⁷ involving first party trusts shows that:

- * statutory and regulatory guidance is limited;
- * in the absence of guidance, courts give excessive deference to public welfare officials and program administrators; and
- * the law continues to wrestle with the concept of disability, retaining vestiges of the outdated idea that all disabilities are alike and that every individual with a disability, regardless of the nature of the disability or the existence of informal supports, requires micromanagement and rigid oversight.

This lack of clarity has had a practical impact on the availability of qualified trustees. In our experience, many capable banks and trust companies – and especially the smaller regional institutions – are second guessing their commitment to the special needs trust market.

As special needs planning attorneys we feel their pain. Perhaps the most challenging aspect of first party trust practice is the lack of credible guidance in the area of administration, leaving the trustee unsure of the criteria being used to measure its

³ 42 U.S.C. §1396p(d)(4)(A), enacted as part of the Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66 (1993) ("OBRA '93").

⁴ EPTL 7-1.12(a)(5)(v).

⁵ *In re Escher*, 94 Misc. 2d 952 (Sur. Ct. Bronx Co. 1978), *aff'd*, 75 AD2d 531 (1st Dep't 1980), *aff'd* 52 N.Y.2d 1006 (1981).

⁶ See, e.g., *In re Morales*, N.Y.L.J., July 28, 1995, at 25 (Sup. Ct., Kings Co. 1995).

⁷ Former New York State Bar Association Elder Law Section Chair David Goldfarb's chapter on supplemental needs trust practice in *Warren's Heaton on Surrogate's Court Practice*, 12-211.12 (Lexis 2018) includes a subchapter entitled "Court-Added Criteria for Supplemental Needs Trusts." The subchapter includes a summary of cases from a variety of New York State courts where judges required modifications to the trust document beyond what is required in our State statute, and which imposed administrative responsibilities on trustees beyond what is required in our state regulations. While the summary is interesting and informative, no credible reading of the cases would leave a practitioner with the impression that there is any uniformity of practice and procedure in New York State.

conduct. Some courts are inclined to micromanage expenditures, others are not. Some rely heavily on the public benefit program representatives' opinions, others do not. Some courts have the personnel to review regular accountings of trust activity, others do not.

This uncertainty is compounded by a blurred line of demarcation between what types of activities should be considered part of the trustee's fiduciary responsibility, and which activities can and should be delegated to outside counsel, private case managers and others.

For their part, given the inconsistent decisional law in this area, court examiners and judges often substitute their judgment for that of the trustee, and default to a generalized and uncircumscribed 'best interest' standard to pick and choose which expenditures are deemed appropriate and which should be disapproved and subject to surcharge. This leaves trustees hesitant to make distributions for fear of being second guessed by someone with little or no firsthand knowledge of the beneficiary's day-to-day circumstances, and fearful of seeking professional assistance out of a concern that those expenditures will be challenged in the future.

Banks and trust companies bear some responsibility for the current state of affairs. Many entered the special needs trust market without much thought to how SNTs differ from other discretionary trusts, and they applied the same administrative and oversight practices to SNTs they used for other trusts.

As a result, in cases where beneficiaries are incapable of self-advocacy and lack any family or informal supports, SNTs often sit dormant. This was the situation in a well-publicized New York case where a professional fiduciary was chastised for failing to take affirmative steps to remain informed about the needs of its autistic beneficiary.⁸ In other cases, the trustees fail to do their due diligence in investigating the availability of government benefits, instead relying exclusively on requests made by family members and guardians. This occurred in a case which received significant attention here in New York,⁹ the result being a substantial surcharge against the fiduciary.

These two well-publicized decisions do not present the professional trustee in a particularly favorable light, justifiably so given the facts of the cases. But they have reinforced the perception that this area of administration is fraught with risk, and as a result many banks and trust companies are reluctant to administer SNTs.

The practical implications are significant and far reaching. The disability community needs credible, capable and competent professional trustees to administer special needs trusts, first party and third party alike. Parents and family caregivers are aging, and when they pass on, siblings and other family members may be unwilling or unable to fill their

⁸ *Matter of the Accounting of JP Morgan Chase Bank, N.A. and H.J.P. as co-Trustees of the Mark C.H. Discretionary Trust of 1995 v. Marie H.* [also referred herein as "Matter of JP Morgan"], 956 N.Y.S.2d 856 (Sur. Ct. N.Y. Co. 2012).

⁹ *Liranzo v. LI Jewish Education/Research*, 28863/1996, *New York Law Journal* 1202609859342 (Sup. Ct. Kings Co. 2013).

shoes. Disability service providers will continue to face cuts in Medicaid and other sources of government funding. It is a simple matter of demographics and public finance: the safety net is not what it once was, and private dollars will be needed to fill in the gaps to ensure that individuals with disabilities do not suffer as a result.

While most attorneys practicing in this area are familiar with the concept of an SNT being a discretionary trust, little has been written on how a trustee's exercise of discretion should be measured in the context of a formal accounting of trust activity. We concentrate on first party trusts in this article because of the greater risk associated with the Medicaid program's right of repayment, but the discussion of an appropriate standard of review for discretionary distributions would apply to both first party and third party trusts.

The first part of this article focuses on the appropriate standard of review for discretionary decisions made by trustees of SNTs. The second part will provide suggestions on how a trustee might satisfy that standard by striking a balance between two credible objectives: (1) the need for court oversight of a trustee who is managing money for a beneficiary who cannot advocate for herself, and (2) deference to the trustee's right to make discretionary decisions which it reasonably believes to be consistent with its fiduciary responsibilities.

III. Developing a Standard of Review for the Administrator of a Supplemental Needs Trust

SNTs are discretionary trusts, but they require trustees in the exercise of discretion to consider the availability of government benefits before deciding to pay privately for a good or service. In New York, our statute allows for the distribution of "net income and/or principal of [the] trust as the trustee shall deem advisable, in his or her *sole and absolute discretion*."¹⁰

When it was enacted in 1993, New York's statute was intended to codify the holding of *Matter of Escher*,¹¹ the first case in New York to support the right of a discretionary trustee to refuse to pay for something that might be available from a publicly funded source (or, in that case, to repay the State for benefits provided in the past). The trustee's ability to exercise discretion was central to the holding in the case, later upheld by the highest court in our State.

New York's statute goes one step further. It allows a drafting attorney to provide the trustee with discretion to make a distribution *even if the distribution causes a reduction in benefits*, so long as the beneficiary will be better off as a result.¹² In exercising this grant of discretion, a trustee must:

1. consider *current* financial eligibility rules, understanding that government benefit eligibility is not static and will continually evolve due to changes in family

¹⁰ EPTL 7-1.12(e)(1)(1).

¹¹ *Supra* n. 5.

¹² EPTL 7-1.12(e)(2)(i)(5).

composition, family financial condition, and beneficiary capabilities and preferences;

2. consider services and supports that are available to the beneficiary as a result of the beneficiary's participation in one or more government funded programs; and
3. ascertain whether services and supports available at the time of a proposed distribution are sufficient to meet the beneficiary's needs and preferences, or whether additional or alternative goods and services should be purchased privately with trust assets. If the latter, the trustee must be able to document the basis for the use of private funds.

But once a trustee has done its due diligence and made the distribution, what standard does a court use to review the trustee's decision to determine whether the distribution should be upheld in a proceeding for settlement of the trustee's accounts? We think the lack of a uniformly accepted answer to this question is the source of much conflict and consternation within the fiduciary community.

A. Federal law does not provide a standard of review

1. The Statute

The federal Medicaid statute 42 USC §1396p(d)(4)(A), provides the underlying foundation for first party trusts. It has four basic requirements: the trust must be established by a parent, grandparent, guardian, a court or by the individual with a disability, the beneficiary must meet the disability criteria under the Social Security Act, the beneficiary must be under the age of sixty-five (65) years at the time the trust is funded with the beneficiary's assets, and the trust must provide that upon the beneficiary's death, State Medicaid programs be repaid for medical assistance provided during the course of the beneficiary's life.

If a first party trust complies with these four criteria, the trust will receive the associated protections under federal Medicaid and Supplemental Security Income (SSI) law: trust assets will be disregarded in determining resource eligibility while the income counting rules of these two programs will determine how a distribution will impact benefit eligibility and amount.

With one important exception, the federal statute leaves fiduciary standards to be determined under the law of the state where the trust was established.¹³ The federal transfer of asset provisions exempt transfers to first party trusts under both 42 USC §§1396 d(4)(A) and d(4)(C) which are established for the "sole benefit" of an individual

¹³ *Lewis v. Alexander*, 685 F.3d 325 (3d Cir. 2012), *cert. denied* 133 S. Ct. 933 (2013), involved the interplay between state trust law and federal Medicaid law. In *Lewis*, the State of Pennsylvania by legislation-imposed limits on pooled special needs trusts not contained in the federal Medicaid statute, including a limit on the trustees' discretion to make various distributions. In striking down all of the State's restrictions other than oversight by the State Attorney General, the Court agreed that the state could supervise special needs trusts, but only in the same manner it supervises all trusts under general state trust law.

with a disability. The term has been interpreted to impose a limitation on distributions, often leading to absurd results.¹⁴ We agree with NAELA Fellow Ron M. Landsman, whose thoughtful analysis leads to the better interpretation of that term: a deviation from the traditional fiduciary obligation to treat all beneficiaries equally, both income beneficiaries and remainder beneficiaries.¹⁵

2. The Regulations

No federal regulations were ever issued in connection with the first party trust provisions of the federal statute.

3. The Administrative Guidelines

The Health Care Financing Administration (“HCFA”, now the Centers for Medicare and Medicaid Services or “CMS”) modified the State Medicaid Manual shortly after the enactment of OBRA ’93 in order to provide guidance to the States in implementing the changes to federal Medicaid law.¹⁶ As it relates to first party trusts, this federal guidance – commonly referred to as “Transmittal 64” – deals primarily with the impact of funding first party trusts on Medicaid eligibility.

The SSI program’s Program Operation Manual System (POMS) contains quite a bit of guidance on how the establishment, funding and administration of trusts might impact eligibility for the SSI program.¹⁷

There is no discussion of a fiduciary standard of review under either set of rules.

B. New York courts have largely ignored the standard suggested in our statute

A reader might assume that SNT administration in New York is well settled in light of the fact that our statute says – clearly and unequivocally – that an SNT trustee has “sole and absolute discretion” to make distribution decisions. The reader would assume that trustee

¹⁴ *In re: Estate of Skinner*, N.C.App.Ct. No. COA15-284 (June 21, 2016), *reversed*, 804 S.E.2d 449 (N.C. S. C. 2017). The Court of Appeals found that the lower court’s reading of the term “sole benefit” as a rigid distribution standard would lead to the “absurd” result of a beneficiary (for whose benefit a home was purchased by the trustee) living in “bizarre isolation.” The Supreme Court reversed the decision of the Court of Appeals because it used the incorrect standard of appellate review.

¹⁵ See Landsman, Ron M., Esq., *When Worlds Collide: State Trust Law and Federal Welfare Programs*, NAELA Journal Volume 10, No. 1 (Spring 2014) for a comprehensive and persuasive piece on this topic. Interestingly, the North Carolina Court of Appeals in *Skinner*, *supra* n. 14., similarly interpreted the term “sole benefit” as a deviation from the traditional standard of loyalty owed to all beneficiaries.

¹⁶ State Medicaid Manual, “Transmittal 64,” General and Categorical Eligibility Requirements, available at <https://www.cms.gov/Regulations-and-Guidance/Guidance/Manuals/Paper-Based-Manuals-Items/CMS021927.html> (last visited September 12, 2018) (see, specifically, section 3259.7).

¹⁷ See recent revisions to the Social Security Administration’s Program Operations Manual System (“POMS”) SI 01120.200 – 203, effective April 30, 2018.

conduct is measured in accordance with long standing New York law governing discretionary trusts.¹⁸ The reader would be mistaken.

New York cases involving first party trusts include personal injury settlements, guardianship proceedings and family court proceedings. Because of the inherently fact specific nature of the cases, they do not provide a reliable and broadly applicable precedent for the drafting and administration of first party trusts.

While there are cases, including from our highest court, which explicitly acknowledge the discretionary nature of SNTs,¹⁹ we are not aware of any decisions which considered a contested distribution from an SNT, acknowledged the trustee's discretion to make a distribution decision, and upheld the distribution notwithstanding the fact that the court might have made a different decision on the same set of facts.²⁰ This level of deference to the trustee of a discretionary trust – qualified by the trustee's responsibility to ensure that its decision is both supportable on the law and facts and is duly documented – is a familiar concept to the seasoned fiduciary.²¹ It underlies the professional fiduciary's willingness to accept an appointment with the understanding that every decision may at some point be called into question.

Many attorneys who represent trustees of SNTs feel as if their clients do not receive the same level of deference, leaving them like fish in a barrel to be speared by the many parties who have standing to second guess: court examiners, judges, public welfare agency attorneys, and disgruntled beneficiaries who may have behavioral and cognitive deficits that make collaborative administration difficult. The fiduciaries' concerns are legitimate.

C. Identifying a standard of review

Most attorneys who represent fiduciaries know that the traditional standard of review for a discretionary trust is the "abuse of discretion" standard. Yet once government benefits and disability are added to the mix, conviction wavers and the analysis becomes diluted.

¹⁸ See Restatement [Third] of Trusts § 50(1)(b); see also *In re Estate of T. Harry Glick*, 2005 N.Y. Misc. LEXIS 7336 (Sur. Ct. Kings Co. 2005) at page 9, citing *In re Gilbert*, 156 Misc. 2d 379 (Sur. Ct. New York Co. 1992); *Trust of Frederick Brockway Gleason, Jr.*, 1999/4582 A, NYLJ 1202629074611, at 1 (Sur. Ct. New York Co. 2013).

¹⁹ *Matter of Abraham XX*, 11 N.Y.3d 429 (2008) at 434.

²⁰ We are unaware of cases undertaking this analysis, with one important exception: the payment of attorney fees. These payments will always be subject to review (at least in New York), regardless of the grant of discretion and regardless of the consent of all interested parties to the amount paid. See *In re Felice*, 1 Misc. 3d 909(A) (Sup. Ct. Suffolk Co. 2004), which specifically addressed a trustee's argument that the supplemental needs trust document deferred to the trustee on attorney fees, and *Stortecky v. Mazzone*, 85 N.Y.2d 518 (1995), which confirmed the right of a probate court to review fees paid by a fiduciary even if all parties to an accounting have agreed and consented.

²¹ See Restatement [Third] of Trusts § 50(1)(b); see also *In re Estate of T. Harry Glick*, *supra* n. 18 at page 9, citing *In re Gilbert*, *supra* n. 18, and *Leigh v. Estate of Leigh*, 55 Misc. 2d 294 (Sup. Ct. New York Co. 1967).

There seem to be two assessment methodologies used by most practitioners, courts and commentators when analyzing distributions from SNTs. One focuses on benefit eligibility, the other uses a broad and uncircumscribed “best interest” analysis. Both assessments are relevant, but neither should be used as a substitute for the “abuse of discretion” standard when reviewing the accounts of the trustee of an SNT.

D. Benefit eligibility is only one factor to consider when making distributions

The language of a “typical” SNT requires consideration of the availability of publicly funded benefits before a distribution is made, with the understanding that the impact of a distribution will vary from program to program.²² Benefit program rules are applied at the time of the distribution, and are based on the beneficiary’s *current* eligibility status. So, for example, the payment of rent by a trustee will impact otherwise similarly situated beneficiaries depending on program eligibility: Medicaid, which in New York allows a trustee to make in-kind payments from an SNT, including for food and shelter, without a reduction in benefits;²³ Supplemental Security Income (SSI), the rules of which typically reduce the benefits of an SSI recipient if a trust pays for food and shelter;²⁴ and Supplemental Nutrition Assistance Program (“SNAP”), formerly Food Stamps, which (in New York) may treat payments to a beneficiary’s household that are permissible for Medicaid purposes as countable income for SNAP purposes, thus reducing the monthly SNAP subsidy.²⁵

It is not uncommon for a distribution to have an adverse impact on one benefit and no impact or limited impact on another. If a trustee decides to pay a beneficiary’s rent, there may be a limited impact on the beneficiary’s SSI payment, no impact on Medicaid eligibility, but a substantial reduction in the SNAP subsidy. If the trustee’s decision to pay rent is reviewed (after the fact as part of an accounting proceeding) based on its impact on government benefits, which benefit program should serve as the baseline in determining the permissibility of the distribution by the trustee?

The answer is “none of them.” Program rules do not restrict or permit a distribution; rather, the rules inform the trustee and beneficiary alike whether the contemplated distribution will have an impact on benefits. The trustee must decide whether a distribution – and the resulting impact on benefits – puts the beneficiary in a better place.

The failure to consider this distinction results in over-reliance on the often *ad hoc* and arbitrary decisions of government benefit agencies, excessive deference to public welfare agency attorneys in court proceedings involving SNTs, and an obsessive focus on

²² EPTL 7-1.12(a)(5)(ii).

²³ 18 N.Y.C.R.R. 360-4.3(e).

²⁴ POMS SI 01120.200E.1.b.

²⁵ *Temporary Assistance (TA) and Food Stamps (FS) Policy: The Treatment of Supplemental Needs Trusts and Reverse Annuity Mortgage (RAM) Loans*, New York State Office of Temporary and Disability Assistance, 01 INF- 8 (March 8, 2001).

informal and non-binding speculation by agency staff who opine on how an issue might be addressed in a future rule or decided in a future controversy. From our perspective, the result is that the tail ends up wagging the dog.²⁶

Perhaps the best example of “excessive deference” can be found in *In re McMullen*,²⁷ a trial court case involving the review of a first party trust as part of a proceeding to settle a personal injury lawsuit. Initially, the decision includes a good explanation of the court’s responsibility to ensure that a proposed trust document meets the statutory criteria for first party trusts such that the beneficiary’s eligibility for Medicaid would be protected.

However, in trying to reconcile a disagreement between the petitioner and the attorney for the local Medicaid agency on the terms of the proposed trust, the court announced a “prophylactic” remedy that would be applied prospectively in all proceedings brought before that Court.²⁸ The ‘remedy’ was to require a petitioner to secure written approval for the terms of a first party trust from the local Medicaid agency before the court would entertain the petition. In other words, the court would require the petitioning party to concede to the demands of the Medicaid program representative - in advance and without the right to be heard - just for the matter to be accepted for consideration.

It is unlikely that such a position would be upheld on appeal (none was taken in the case), and one can understand why a court with little statutory guidance and without competent advocacy by special needs trust counsel would try to fashion a remedy to streamline future proceedings. But the case is badly decided.

Another recent New York decision, *Matter of Tinsmon* ²⁹, illustrates how public welfare agency attorneys try to use program rules to control and limit fiduciary conduct. In *Tinsmon*, individual co-trustees of a first party trust sought court approval to use trust funds to purchase a one-half interest in the primary residence of the beneficiary, an SSI recipient. The beneficiary already owned the other one-half interest outright. The trust did not require prior court approval, but the co-trustees were also the parents and court appointed guardians. More important, the one-half interest was owned by one of the co-trustees who had helped the beneficiary finance the purchase prior to the injury.

²⁶ Consider the April 2018 release of the revisions to the POMS on SNTs, *supra* n. 17. Most special needs trust practitioners would agree that the changes were favorable and provided much needed clarity. But they only involve one agency’s interpretation of how a distribution or investment by a trustee might impact the benefits the agency provides. They do not create distribution and administration standards that are applicable across all SNTs, and yet our impression is that many special needs planning attorneys treat them this way. The result is a misplaced and outsized emphasis on that agency’s often inconsistent and arbitrary application of its own rules.

²⁷ *In re McMullen*, 166 Misc.2d 117 (Sup. Ct., Suffolk Co. 1995).

²⁸ *Id.* at 121.

²⁹ *Matter of Tinsmon (Lasher)*, 79 N.Y.S. 3d 854 (Sur. Ct., Albany Co. 2018), *aff’d* 169 AD3d 1305 (Third Dept. 2019).

The co-trustees asked the court to approve the ‘buy out’ of the co-trustee’s interest and, in effect, a distribution of the interest to the beneficiary, outright and free of trust, with the result being that the beneficiary would own the entire residence. The beneficiary was a young mother, and by leaving the home in her name, upon her death her interest would pass to her children without Medicaid estate recovery for expenses incurred prior to age 55.³⁰

The local Medicaid agency was served with process because of the Medicaid program’s right of recovery at death and – predictably - objected. The agency argued, among other things, that the transaction was prohibited under the POMS.

There is no such prohibition under the POMS. The POMS clearly contemplate that a trustee may use trust assets to purchase an item which would be exempt in determining SSI eligibility if owned by the beneficiary outright,³¹ a point made clear by the guardian *ad litem* who represented the beneficiary in the transaction. The guardian *ad litem* recommended that the transaction proceed as proposed, and the Court ultimately approved. The Medicaid agency appealed the decision, which was upheld by the appellate court.³²

But what if there was an adverse impact on SSI? So long as the trustee determined that the beneficiary would be left in a better position notwithstanding, the terms of the trust and the language of New York’s statute give the trustee the discretion to proceed nonetheless. Benefit eligibility is just one factor to consider in the exercise of discretion; it does not independently permit or preclude a discretionary distribution.

E. "Best Interest" is another factor to consider, and should not be used as a substitute for the traditional standard of review

Courts considering the disposition of litigation settlements and guardianship property will render decisions based on what they determine to be in the “best interest” of the unemancipated minor or person with a disability. Predictably, decisional law in this area tends to be very fact specific, and commonly recites the courts’ responsibility to protect those who are unable to speak for themselves.³³

A best interest assessment is properly undertaken when a trust arrangement is being recommended to a court. Whether the use of a trust (versus some other custodial arrangement) is appropriate, whether the proposed trustee is acceptable, and whether the terms of the proposed trust are consistent with the objectives and concerns of the

³⁰ 42 U.S.C. §1396p(b)(1)(B).

³¹ POMS SI 01120.201(I)(1)(c).

³² *Supra* n. 29.

³³ N.Y. Surrogate’s Court Procedure Act (SCPA) 1713 (“reasonable, proper and just under the circumstances”); *Dinnigan v. ABC Corp.*, 35 Misc. 3d 1216(A) (Sup. Ct. New York Co. 2012); *Matter of Teitelbaum*, 11 Misc.3d 1067(A) (Sur. Ct. Rockland Co. 2006).

court should all be viewed through the “best interest” lens at the time the arrangement is being proposed.

The most frequently cited example of this practice in New York is in the *Matter of Morales*, where a court-appointed guardian sought to transfer litigation proceeds to a first party trust to protect benefit eligibility. Explaining that “the duties and responsibilities of the trustee to the incapacitated person are akin to those of a guardian,” the court went on to require modifications to the language of the proposed document which it “deem[ed] necessary to protect the interests of the disabled person.”³⁴ The judge then provided – right in the language of the decision – a sample trust document to be used as a “guide to the bar” for drafting first party trusts.

The “Morales Trust” document provided by the court includes provisions not required as a matter of statutory law and which many practitioners believe to be overly restrictive. The decision should be understood to provide guidance only in cases involving the establishment of SNTs in guardianship proceedings. But many New York courts continue to follow it in other types of proceedings when funding an SNT is proposed.

In the context of the *establishment and funding of an SNT*, the parties understand the rules of the game. The court must decide *whether* the SNT should be established, *who* should serve as trustee, and *how* the trust should be drafted to address the court’s specific concerns in that particular case. Counsel have their opportunity to argue against modifications they believe exceed the statutory mandate or which are not necessary given the facts of that case, and ultimately the court will render its decision based on what it believes to be in the best interests of the individual before it.

But the question presented here is a different one: once an SNT has been established and funded in accordance with a court’s best interest determination (or even in those cases where the SNT is established independently and without court involvement), what is the standard of review to be applied by a court when reviewing distributions made by the trustee? Little decisional law exists in New York, but one well publicized case illustrates the approach taken by most courts in our experience.

In *Matter of Liranzo*³⁵ the corporate trustee of a first party trust funded with litigation proceeds sought to settle its account and terminate the trust. The trust was initially funded with just over \$420,000. Six years later, the trust had approximately \$3,200 remaining. The accounting showed that most of the money was used to pay for private caregivers and taxi service for the beneficiary.

The decision begins with the judge’s conclusion that the trustee breached a number of commonly understood, generalized rules of fiduciary conduct (the “duty of undivided loyalty,” the obligation to administer the trust in the “sole interests of the beneficiary,” and

³⁴ *In re Morales*, *supra* n. 6.

³⁵ *Liranzo*, *supra* n. 9.

the need to “act reasonably and in good faith”). But the decision goes on to recite concepts that are less precise (criticism of distributions that “could have either been avoided or were unreasonable,” the failure to “provide support for the plaintiff for as long as possible,” and “authorizing each and every discretionary disbursement requested by the infant plaintiff’s mother”³⁶).

In addressing the private caregiver payments, the judge criticized the trustee for accepting the mother’s claim, supported by a private social worker, that the beneficiary was better off with private caregivers as opposed to Medicaid funded aides. This was not sufficient for the judge, who wrote that “the trust agreement requires that a good faith effort be made by the trustee to inquire about providers of home healthcare whose costs are covered under Medicaid.”

The court also penalized the trustee for spending more than \$50,000 on private taxi services based on the mother’s representation that driving in a taxi was a form of therapy for the beneficiary. In the words of the judge, the trustee “should have further investigated before allowing the disbursements. This “taxi therapy” does not appear to be a responsible use of Trust fund monies consistent with prolonging the life of the Trust.”³⁷

A trustee might be able to work with the court’s analysis of caregiver expenses, as the decision suggests that an investigation of Medicaid funded alternatives might have saved those distributions from surcharge. But testimony did show that the mother and a social worker were consulted prior to making the discretionary decision to pay privately for that care. Is that not a “good faith effort”? Was the issue the lack of independent inquiry by the trustee or a matter of inadequate documentation?

The court’s analysis of the taxi expenses is more troubling. The statement that the expense “does not appear to be a responsible use of trust funds” is vague. Taxi therapy *did* appear to be responsible in the mother’s eyes and in the eyes of the social worker. If the expense was hippotherapy would that have made a difference? And who better to make that assessment than the primary caregiver and a professional advocate?

Had the court articulated a clear standard of review to be applied to each trust expense, the decision would be more helpful. Instead, the judge substituted her judgment for that of the trustee as to what types of expenditures were in the best interest of the beneficiary, relying primarily on generalized statements of fiduciary responsibility to support her decision.

In the end the court refused to approve the private caregiver and taxi expenses (and a few others as well), resulting in a surcharge of over \$170,000. Admittedly, when a trust with well over \$400,000 is almost fully depleted in six years it does not bode well for the trustee. But egregious facts should not relieve the court of its responsibility to frame its

³⁶ *Id.* at p. 4.

³⁷ *Id.* at p. 7.

surcharge and write its decision in a manner that leaves the parties with a clear understanding of the criteria being used to measure conduct.

What trustees need is a workable methodology for analyzing distributions – be they modest or significant, mundane or out-of-the-ordinary - once an SNT is up and running. The first step in developing such a methodology is an agreement on the correct standard of review.

F. Abuse of discretion is the correct and the only workable standard of review to be applied when assessing distributions from special needs trusts.

The abuse of discretion standard is the traditional standard applied to the conduct of all discretionary trustees under New York law,³⁸ and is also consistent with a recent line of New York cases which take the position that SNTs should be treated no differently than other irrevocable trusts established under state law.³⁹

The abuse of discretion standard is the only standard which can comfortably incorporate the legitimate objectives of the benefit eligibility assessment and the best interest assessment. Under the abuse of discretion standard, the trustee must consider the impact on eligibility and services (the benefit eligibility assessment) and the resulting benefit to the beneficiary (the best interest assessment) when making a distribution decision. Once these two factors have been reviewed, considered and documented and the distribution has been made, a reviewing court should defer to the trustee and approve the distribution unless the trustee abused its discretion by acting in bad faith or beyond the bounds of reasonable judgement.⁴⁰

The abuse of discretion standard does not provide a ‘pass’ to the trustee of an SNT any more than it provides a pass to trustees of other types of discretionary trusts. All of the traditional obligations of fiduciary conduct would still apply: the need to invest prudently, the need to account in detail, the prohibition against self-dealing, etc. But the abuse of discretion standard will protect the trustee who has complied with the traditional obligations of fiduciary conduct, and who can demonstrate that it has done its due diligence in considering a beneficiary’s benefit eligibility and best interest when making a distribution decision.

³⁸ *Supra* n. 18. In fact, the trustee’s discretion as granted under the terms of a will drafted decades ago was a critical part of the court’s analysis in the seminal case on special (supplemental) needs trusts in New York, *In re Escher supra* n. 5.

³⁹ *Matter of Kaidirmouglou*, N.Y.L.J. November 5, 2004, at page 28 (Sur. Ct. Suffolk Co. 2004); *Matter of KeyBank*, 58 Misc.3d 235 (Sur. Ct. Saratoga Co. 2017); *Matter of Feuerstein*, 147 A.D.3d 688 (1st Dep’t 2017). New York attorneys are well advised to remember that even a wholesale adoption of the ‘abuse of discretion’ standard in evaluating distributions from all supplemental needs trusts will not shield attorney fees from later scrutiny. *Matter of Felice, supra* n. 20.

⁴⁰ *Trust of Frederick Brockway Gleason, Jr.*, 1999/4582 A, N.Y.L.J. 1202629074611, at *1 (Sur. Ct. New York Co. 2013).

Adoption of the abuse of discretion standard would help address many of the concerns of banks and other professional fiduciaries about assuming trusteeship of first party (and even third party) special needs trusts, and it would encourage more capable and credible institutions to offer their services to individuals with disabilities and their families. If clients prefer to use family members or other individuals as trustees, counsel can advise that their conduct will be measured in a fair and understandable way.

IV: Developing a Protocol for Administration Under the Abuse of Discretion Standard

The abuse of discretion standard provides the flexibility and protection afforded the trustees of other discretionary trusts so long as the trustee follows the commonly accepted rules of fiduciary conduct, as supplemented by additional steps that acknowledge the beneficiary's disability and eligibility for government benefits.

To obtain the protection afforded to trustees of other discretionary trusts, the SNT trustee should acknowledge and address three aspects of SNT administration that are not at issue in the administration of other discretionary trusts:

1. A beneficiary's cognitive disability may prevent reliable communication with the trustee,
2. Programs and services available to support the beneficiary in the community represent an additional resource to be considered before using trust funds to purchase a good or service, and
3. Traditional, informal means of settling accounts may be insufficiently protective.

Effective SNT administration requires the trustee to establish a means of communication with the beneficiary or a beneficiary's representative, a protocol for assessing programs and services, and a plan for regular accounting and periodic settlement. If followed, and presuming that the trustee has satisfied the other, traditional obligations of fiduciary conduct, the trustee's reasonable exercise of discretion should be supported upon judicial review under an abuse of discretion analysis, even if the court would have made a different decision on the same set of facts.

A. Basic rules of fiduciary conduct applicable to all trustees

All trustees must follow the basic rules of fiduciary conduct, requiring them to apply income and principal in accordance with the terms of the governing document,⁴¹ account for the application of principal and income,⁴² invest prudently and in accordance with the

⁴¹ New York Estates Powers & Trusts Law (EPTL) 11-1.1(a)(2).

⁴² *Matter of Francis*, 19 Misc. 3d 536 (Sur. Ct., Westchester County 2008).

terms of the trust,⁴³ prepare and file tax returns,⁴⁴ and keep beneficiaries informed of how trust funds are being invested and/or utilized.⁴⁵

B. Exercising discretion

Trustees of discretionary trusts must use judgment when making distribution decisions. In New York, case law follows a few common lines of inquiry in determining whether a trustee properly exercised discretion:

1. Does the trustee have an established process for review and consideration of beneficiary requests?⁴⁶ In other words, is there evidence that the trustee is making informed decisions?

2. Did the trustee follow its own established policies in making distribution decisions, and did it document the basis for those decisions?⁴⁷

3. Did the trustee exercise independent judgment rather than deferring to a beneficiary or a beneficiary's representative?⁴⁸

4. Does the document require the trustee to consider whether the beneficiary had other assets and resources that could be used in lieu of using funds from the trust, and if so, did the trustee do so?⁴⁹

5. For significant or long-term expenditures, did the trustee balance the immediate needs of the beneficiary with probable future needs?⁵⁰

If the trustee can answer these questions in the affirmative, courts will typically support the trustee's discretionary decisions even if the judge or another party to the proceeding might have made a different decision on the same set of facts. In the realm of discretionary trusteeship, the process of proactive administration protects the fiduciary and beneficiary alike. When the trustee follows the process of communication, investigation, consideration and documentation, the beneficiary receives the benefits of the fiduciary arrangement. In exchange, the trustee is protected from later challenge to its distribution decisions simply because another might have reached a different conclusion.

This *quid pro quo* assumes that both the trustee and the beneficiary are capable of self-advocacy. But when a beneficiary has a cognitive disability, she is at a disadvantage.

⁴³ EPTL 11-2.3 ("Prudent Investor Act").

⁴⁴ New York Tax Law § 651(a)(2).

⁴⁵ *Matter of Spacek*, 45 Misc. 3d 1210(A) (Sur. Ct. Nassau County 2014), *aff'd*, 155 AD3d 747 (2d Dep't. 2017).

⁴⁶ *Matter of Ralph Manny*, 2010 N.Y.L.J. LEXIS 4508 (Sur. Ct. Westchester County 2010).

⁴⁷ *In re: Judicial Settlement of the Account of Bank of Am., N.A.*, 2013 N.Y.L.J. LEXIS 2388 (Sur. Ct., N.Y. Co. 2013).

⁴⁸ *Matter of Hammerschlag*, 2001-3772, NYLJ 1202597358371 (Sur. Ct., New York Co. 2013).

⁴⁹ *In re Levison's Will*, 29 Misc. 2d 697 Sur. Ct. Rockland County 1961); *Matter of McDonald (Luppino)*, 100 A.D. 3d 1349 (2012).

⁵⁰ *Estate of T. Harry Glick*, *supra* n. 18.

Courts struggle to find the correct balance between oversight for the benefit of those who cannot fully advocate for themselves and the well-established body of law which protects a fiduciary's authority to make discretionary decisions.

C. Disability and discretion

Supplemental Needs Trusts are discretionary trusts⁵¹ for a reason. These trusts often have to last for the lifetime of a beneficiary with a disability. Circumstances change, and the authority to exercise discretion allows the trustee to respond to changes in need.

Where a beneficiary is unable to adequately advocate for herself because of a cognitive disability, courts have a responsibility to provide oversight.⁵² In proceedings for the establishment of supplemental needs trusts in New York, this equitable authority is often cited as justification for imposing administrative obligations on the trustee that are above and beyond what the federal and state statutes would otherwise require.⁵³ So, for example, even though there is no statutory or regulatory or administrative requirement that the trustee of a supplemental needs trust prepare annual accountings, guardianship courts often impose such a requirement in order to protect a beneficiary who is incapable of self-advocacy.

No one would question the courts' *parens patriae* responsibility to protect the interests of those who cannot protect themselves. But simply reciting the obligation does not provide any practical administrative guidance to the trustee of a discretionary trust. In the context of SNT administration, the question is not whether a court has the authority to protect the interests of a beneficiary with a disability. The question is how that protection is provided.

D. Court reluctance to substitute judgment

Courts typically do not substitute their judgment for that of a trustee so long as the trustee's exercise of discretion was reasonable, consistent with the terms of the trust, and made in good faith.⁵⁴ Courts often refuse to provide guidance when the trust document gives the trustee the responsibility to make a discretionary decision.⁵⁵ This narrow role

⁵¹ New York's statute defines a supplemental needs trust as "a discretionary trust established for the benefit of a person with a severe and chronic or persistent disability." EPTL 7-1.12(a)(5).

⁵² *In re Goldblatt*, F (Sur. Ct., Nassau County 1994); *Cano v. Shmonie Corp.*, 2004 N.Y.L.J. LEXIS 3059 (Sup. Ct., Bronx County 2004). The decision in *Cano* is a good illustration of the difficulty that courts have in drawing a line of demarcation between guardianship oversight and discretionary trusteeship.

⁵³ *In re Morales*, *supra* n. 6; *Cano v. Shmonie Corp.*, *supra* n. 52.

⁵⁴ "The rule is so well established that it may be said to be fundamental and elemental that courts will not substitute their judgment for the discretion fairly exercised which is lawfully reposed in officials, courts or tribunals. This rule has long been applied to the office of executor and trustee." *In re Estate of Messer*, 34 Misc. 2d 416 (Sur. Ct., Cattaraugus Co. 1962) at p. 8; see also *Estate of T. Harry Glick*, *supra* n. 18; *In re William M. Kline Revocable Trust*, 196 Misc. 2d 66 (Sur. Ct., Fulton County 2003); *In re: Judicial Settlement of the Account of Bank of Am., N.A.*, *supra* n. 47.

⁵⁵ *Matter of Sheppard*, 147 AD3d 1239 (3d Dep't 2017).

for the courts is codified by statute in New York, where courts render "advice and direction" in a limited number of enumerated situations.⁵⁶

This structure breaks down when cognitive disability enters the picture. Courts are reluctant to defer to the discretion of the trustee and often substitute their judgment when reviewing discretionary distributions.⁵⁷ The net effect is that trustees – unsure of how their discretionary decisions will be measured – are often reluctant to make any significant distributions, or refuse to do so without regular input from a court.

This is precisely the type of micromanagement that a discretionary trust is intended to avoid.⁵⁸ A beneficiary's disability is no reason to deviate from the standard practice of deferring to the trustee's judgment, so long as the trustee has not abused its discretion. Under an "abuse of discretion" analysis, if the trustee of an SNT follows the traditional rules governing trustee conduct, the trustee's exercise of discretion should be upheld even if a court would have made a different decision on the same set of facts.

E. Establishing a protocol for communication with a beneficiary

Trustees need information to make *informed* discretionary decisions. In a typical administration, the trustee can communicate directly with an adult beneficiary, and in the case of a minor a trustee can communicate with a legally responsible adult such as a parent. Communication is relatively straightforward and unencumbered.

SNT beneficiaries may lack the ability to communicate. They may not have court appointed guardians or voluntarily designated agents under power of attorney. They may lack informal supports like family members and friends, or those informal supports may be unreliable or dishonest.

These practical challenges defy simple solution. If a beneficiary with a developmental disability needs a winter coat, the trustee may have the authority to purchase the coat, and the purchase may be an appropriate exercise of discretion. But how would the trustee know that the beneficiary needs a coat? How does the trustee buy an appropriate coat? How does the trustee get the information it needs to appropriately exercise its discretion and facilitate the purchase?

1. Identifying Sources of Information:

⁵⁶ New York Surrogate's Court Procedure Act (SCPA) § 2107.

⁵⁷ See *Cano v. Shmonie Corp*, *supra* n. 52. See also *Liranzo*, *supra* n. 9. In *Liranzo*, the Court did not specifically articulate a standard of review; rather, the authors read the decision as applying a substituted judgment analysis, as various criteria are cited in the decision. One may also read decisions allowing for the review of counsel fees paid by trustees of SNTs as undermining the trustee's discretion because of a beneficiary's disability. See, e.g., *In re Examination of the Annual Inventory & Account of Susan Felice & the Bank of N.Y.*, 2003 N.Y. Misc. LEXIS 990 (Sup. Ct., Suffolk Co. 2003).

⁵⁸ Some transactions should require court approval, such as the use of funds in a trust for a minor to purchase a home where the minor will live with the family. But in New York, this transaction is contemplated in our advice and direction statute, based on the potential conflict of interest.

Family members might be able and willing to provide relevant information. But what if the beneficiary has no reliable family members (or no *honest* family members), no court appointed guardian, and no other reliable, informal advocates?

SNT beneficiaries might have Medicaid funded staff to provide this information, but the continued erosion of Medicaid funding for this type of service has made this a less reliable option. Medicaid funded care managers have increased caseloads, and disability provider agencies face high staff turnover (or are simply unable to locate staff in the first place). As a result, the trustee's affirmative obligation to make informed discretionary decisions⁵⁹ often cannot be met through communication with Medicaid funded staff alone.

If there are no credible family supports, no court appointed guardian, and no reliable Medicaid funded staff, the trustee should consider retaining a private care manager, social worker or other advocate to serve as its "boots on the ground" to obtain information that the trustee can consider when making a distribution decision.

2. Recommendation:

In determining whether a trustee of a supplemental needs trust reasonably exercised discretion, judicial review should consider whether the trustee established an effective protocol for communication and a credible means of obtaining reliable information about the beneficiary's needs.

Upon being appointed the trustee should undertake the following analysis:

1. Is the beneficiary competent to correspond and advocate directly? Many SNT beneficiaries with physical disabilities are fully capable of communicating directly with the trustee.
2. If the beneficiary cannot communicate directly, is there a court appointed guardian or agent under power of attorney who is able to speak reliably on behalf of the beneficiary and provide important information and documentation?⁶⁰
3. Is the beneficiary supported by reliable⁶¹ family members, friends or other informal advocates? While the trustee may be precluded from sharing information about the trust with individuals who lack legal authority to access it, the trustee is free to *receive* information from any credible source, supplementing whatever other information the trustee receives.

⁵⁹ "Once the trustees were required to make themselves knowledgeable about [the beneficiary's] condition and his needs, and the availability of services that would enable them to provide for those needs, they began, and continue to use funds from his trust for the purposes [the testator] anticipated and so deeply desired.." *Matter of JP Morgan Chase Bank N.A. (Marie H.)* [also referred to herein as "*Matter of JP Morgan*"], *supra* n. 8.

⁶⁰ If all else fails, a trustee has the authority (in New York) to apply to a court for the appointment of a professional guardian who would have authority to obtain information and provide documentation that a trustee would need to make informed decisions. N.Y. Mental Hygiene Law § 1.06(a)(4).

⁶¹ Whether a family member is "reliable" is also a judgment call.

4. Does the beneficiary have program staff who could help communicate requests for goods and services to supplement what government benefit programs provide?
5. Can the trustee hire a private care manager or other advocate to provide periodic assessments and recommendations for distributions?⁶²

F. Developing a process for assessing and reviewing programs and services

Professional trustees are required to have a basic knowledge and understanding of the rules governing investments, income taxes, and other financial issues common to all fiduciary appointments. Most institutions have a process in place to review these issues on a regular basis.

When an issue falls outside of a trustee's traditional area of expertise, trust documents are typically written to allow the trustee to retain outside professionals and to pay those professionals with trust funds. For example, fiduciaries often retain outside professionals to address complicated tax questions. The reasonableness of the fee paid is always subject to review on an accounting, but the authority to retain outside expertise is well established.⁶³

SNTs – by their terms and by statute – require a trustee to consider factors that are outside the traditional realms of trustee expertise: the availability of public benefits and the means tested goods and services they provide, the adequacy of those goods and services, and the potential impact of a distribution on continuing eligibility.⁶⁴

This requirement is a variation on a common theme found in cases analyzing a trustee's exercise of discretion. Government benefit programs represent a valuable source of funding for goods or services that the trustee must consider before making a discretionary distribution.⁶⁵ To adequately consider these other sources, the trustee must answer a few questions.

1. Determining whether Medicaid (or another program) pays for a good or service.

⁶² This was the recommendation of the court in *Matter of JP Morgan*, *supra* n. 8. It is important to note that the beneficiary resided in a residential program with 24-hour Medicaid funded staffing. *Matter of JP Morgan* at p. 369. The case illustrates the fact that a trustee's obligation to remain informed goes beyond simply ensuring that a beneficiary is participating in a Medicaid funded program, and requires independent assessment and review.

⁶³ *Matter of U.S. Bank N.A.*, 51 Misc. 3d 273 (2015).

⁶⁴ New York's statute defines a supplemental needs trust as a discretionary trust which, by its terms "prohibits the trustee from expending or distributing trust assets in any way which may supplant, impair or diminish government benefits or assistance for which the beneficiary may otherwise be eligible or which the beneficiary may be receiving; provided, however, that the trustee may be authorized to make such distributions to third parties to meet the beneficiary's needs for food, clothing, shelter or health care but only if the trustee determines...that the beneficiary's basic needs will be better met if such distribution is made." EPTL 7-1.12(a)(5)(ii).

⁶⁵ *In re Levison's Will*, *supra* n. 49. Decisional law in this area focuses on the trust creator's intentions in determining whether the trustee should consider a beneficiary's other resources when making a discretionary distribution. There is no ambiguity with an SNT, as the requirement to consider other resources (government benefits) is written into the New York statute and the language of the document.

This requires more than simply asking, "Is the beneficiary Medicaid eligible?" Medicaid is a payment source for certain goods and services, but the question for the trustee is whether Medicaid will pay for the specific good or service that the beneficiary needs. It is not uncommon for a beneficiary to be eligible for Medicaid (meaning that the Medicaid program is willing to pay for a good or service), but the good or service itself may be unavailable. This dilemma is often seen in the area of Medicaid funded staffing, where the hourly rate paid to community-based staff is so low that service providers either cannot find people to fill the positions, or they are forced to hire individuals with minimal experience.⁶⁶

Medicaid funded waiver⁶⁷ programs offer a broad range of services to beneficiaries, some with more generous housing supports, and others with better hourly reimbursement rates for staff. But it is the responsibility of the beneficiary (or the beneficiary's family or staff) to ensure that those services are being fully utilized. In our experience, parents and other family members spend so much time and effort simply managing the affairs of the person with the disability that they have neither the time nor the inclination to develop a comprehensive understanding of program requirements. And if staff are overworked, underpaid or inexperienced, they will be minimally resourceful. Available services often go underutilized.

2. Assessing whether the government funded option is adequate, or whether trust funds should be used to supplement or replace it.

In order to comply with the terms of the trust and (in New York) the language of the governing statute, the trustee of a supplemental needs trust must determine whether funds in the trust should be used to *supplement* (or supplant) an available good or service.

Consider a beneficiary in need of a wheelchair. Medicaid pays for a basic wheelchair, but the beneficiary might do better with a more expensive wheelchair that is a better fit for her needs – safer, more comfortable, with more sophisticated positioning systems and other controls. The trustee might be able to acquire the chair immediately and without having to go through the Medicaid program's administrative review and approval process. The trustee has the discretion to pay for the better chair.

Consider a beneficiary with Medicaid funded staffing in the home. A beneficiary may be approved for three hours per day, two days per week. But the beneficiary and her family would rather not work with inexperienced Medicaid-funded staff, or they may want more

⁶⁶ In New York the issue has reached critical proportions. See testimony of Mark Van Voorst, Executive Director of NYSARC before the New York State Legislature warning of the impending crisis. <https://bfair2directcare.com/2019/02/07/the-arc-new-york-executive-director-mark-van-voorst-asks-new-york-state-do-we-need-a-tragedy-to-occur-before-you-will-fund-a-living-wage-for-direct-support-professionals/>.

⁶⁷ Medicaid Waiver programs provide services to people who would otherwise be in an institution, nursing home, or hospital, allowing them to receive Medicaid funded long-term care in the community. <https://www.medicaid.gov/medicaid/hcbs/authorities/1915-c/index.html>.

hours of coverage. If there are funds in the trust to pay, then the trustee has the discretion to purchase those extra hours, or hire other, more experienced staff.

Before using trust assets to *supplement* (or supplant) a government funded good or service, the trustee should have some process in place to confirm what the program is providing, and some means of documenting that the beneficiary would benefit from other or additional goods or services.

3. Determining whether using trust funds used to pay for a good or service will negatively impact benefit program eligibility.

Programs such as the Supplemental Security Income ("SSI") and Supplemental Nutritional Assistance Program ("SNAP") provide direct financial benefits to their participants. Others – like Medicaid – provide a payment source for goods and services, but do not make payments directly to a beneficiary.

The same distribution from an SNT can impact different programs in different ways. For example, the payment of rent from a trust will have no impact on Medicaid⁶⁸ but may result in a reduction in a monthly SSI payment and an increase in the rent paid for HUD subsidized housing.⁶⁹

The trustee is charged with knowing which benefit programs a beneficiary is participating in *at the time of the distribution*, understanding that many beneficiaries migrate in and out of different benefit programs based on changes in family composition, financial condition, and other circumstances, and knowing how the proposed distribution might impact those benefits.⁷⁰

If a trustee exercises discretion and uses funds in the trust to pay rent so that the beneficiary can move into a nicer neighborhood, the trustee must understand the impact of its discretionary distribution on the SSI benefit, and document why the beneficiary would be better off with less monthly income but a better place to live.

4. Recommendation:

In determining whether a trustee of a supplemental needs trust has reasonably exercised discretion, judicial review should consider whether the trustee developed a protocol for assessing government benefits and available services, and a process for periodic review and update.

⁶⁸ 18 N.Y.C.R.R. § 360-4.3(e).

⁶⁹ POMS SI 01120.200E.1.b; *see also The Impact of Special Needs Trusts on Eligibility for Subsidized Housing*, The Voice, Volume 5, Issue 4 (March 2011), <https://www.specialneedsalliance.org/the-voice/the-impact-of-special-needs-trusts-on-eligibility-for-subsidized-housing-2/>.

⁷⁰ New York's statute makes clear that "neither principal nor income held in trust shall be deemed an available resource to the beneficiary under any program of government benefits or assistance; however, *actual distributions from the trust may be considered to be income or resources of the beneficiary to the extent provided by the terms of any such program.*" EPTL 7-1.12(b)(3) (emphasis added).

Upon being appointed the trustee should promptly develop a plan to confirm government benefit eligibility and available goods and services, to assess whether those services and supports are adequate, and to review that information on a regular basis. The trustee should consider the following resources and suggestions:

1. For beneficiaries participating in a waiver program, disability service providers prepare periodic reports (called Service Plans or Life Plans in New York⁷¹) which include information on a beneficiary's preferences, health, family supports, and professional providers. Different programs have different reporting requirements, but most publicly funded programs will require a summary report of some type. These reports can often provide useful information on what services might be available through a government benefit program.⁷² The trustee should regularly obtain these reports.
2. If a beneficiary has proactive and well-informed family members, they may be able to provide the trustee with information needed to determine whether a government benefit program is providing an adequate level of goods and services.
3. The trustee can hire a private care manager or other advocate to conduct a comprehensive review of benefit eligibility and available services and provide options for supplementing those benefits and supports.⁷³

G. Preparing annual accountings and periodically seeking judicial settlement

At some point, every trustee seeking to be discharged must account to its beneficiaries. If those beneficiaries are competent and willing, they can "settle" the trustee's accounting voluntarily and without court order. This is often not an option for SNT trustees.

1. What is an "accounting"?

We use the term "accounting" to refer to a summary of financial activity over a given time period, presented to the beneficiaries of a trust to keep them informed about trust activity. Sometimes they are filed with a court, sometimes not.

Some courts provide forms that trustees must use in summarizing financial activity. Some court forms are very simple, requesting only opening and ending balances and a summary of distributions made over the accounting year. Others are more elaborate and

⁷¹ For individuals served by the NYS Office of People With Developmental Disabilities, see Administrative Directive 18 ADM 06, "Transition to People First Care Coordination" (June 26, 2018).

⁷² A word of caution is warranted here. Those with experience reviewing Life Plans (formerly called "Individualized Service Plans" or "ISPs") know that these documents often contain outdated and inaccurate information, largely a result of staff having too many reports to prepare and not enough time and experience to prepare them in a thorough and detailed fashion.

⁷³ In 2016, the New York State Bar Association Trust and Estates Section Subcommittee Reviewing Changes to EPTL 7-1.12 recommended that the statute be modified so as to require the trustee of a supplemental needs trust to investigate the need for a case manager, to retain a case manager where necessary, and to pay the case manager from trust funds. See Memorandum dated March 30, 2016, from Nina P. Silfen, Esq. Stephanie Hamberger, Esq., and Jonathan Byer, Esq. to Michael Schwartz, Esq., Chair of the Trust and Estate Administration Committee of the Trusts and Estates Section of the New York State Bar Association.

track unrealized gain and loss, allocate expenses to principal and income, and allow the trustee to provide additional information on explanatory schedules.

Used here, the term "informal accounting" refers to accountings which are filed with a court or presented to a beneficiary for informational purposes. In some cases, they are required by statute, by court order or by the terms of the trust document. In others they are not required but are prepared voluntarily by a trustee to keep the beneficiaries informed of trust activity.

In New York, many SNT trustees are required to file annual informal accountings when the trusts were established and funded by court order in a guardianship proceeding or personal injury action. These informal accountings are reviewed by an examiner or fiduciary clerk, but they will not receive formal judicial review. We refer to them as informal accountings even though they are filed with a court.

The format used for an informal accounting can vary. A year-end financial statement that a trustee provides to a beneficiary could be considered an informal accounting. A checkbook ledger and accompanying bank statements might be appropriate in some circumstances. If a trustee is required to account by court order and the court has a preferred form, then the trustee will use that form. If there is no court filing requirement, a trustee wishing to keep its beneficiaries informed of trust activity can use whatever form it deems appropriate. Some trustees may send financial statements, others may use a more elaborate format similar to what would be used in an estate accounting.

A proceeding for "judicial settlement" involves a petition to a court asking for review and approval of the trustee's accounting. These proceedings are filed with notice to all interested parties. In New York, the form of the accounting which must accompany the petition is promulgated by the Chief Administrator of the State of New York and is comprehensive.⁷⁴

2. Accounting requirements for SNTs vary by state.

There is no requirement under the federal or many state supplemental needs trusts statutes that a trustee prepare annual accountings of any type or with any frequency. Such is the case in New York, where there is no statutory, regulatory or administrative requirement that a trustee of an SNT prepare annual accountings.⁷⁵ As a result, many first party and third party SNTs in New York and elsewhere are administered without ongoing oversight. If the trustee wants to resign during the beneficiary's life or seeks to have its accounts settled upon the beneficiary's death, the trustee's discretionary decisions will be subject to second guessing inherent in proceedings for judicial settlement of multi-year accountings, a process familiar to trustees of discretionary trusts.

The proactive trustee can mitigate the risk of belated challenge by keeping the beneficiaries regularly informed of trust activity, but the effectiveness of this approach will

⁷⁴ SCPA 106; Official Form JA-4, "Trust Accounting With Instructions."

⁷⁵ *Matter of Kaidirmoglou*, *supra* n. 39; *Matter of KeyBank*, *supra* n. 39; *Matter of Feuerstein*, *supra* n. 39.

be determined in part by the accounting format used, the frequency of the disclosure, and the capacity of the beneficiary.

3. Financial statements alone provide insufficient disclosure.

In a traditional trust administration, the trustee provides a beneficiary with monthly, quarterly or annual financial statements. These statements keep the beneficiaries informed and can serve as the basis for an informal settlement of the trustee's accounts when the trust terminates or when a trustee is otherwise seeking to be released.

This level of informality is inappropriate in the context of SNT administration for at least four reasons:

1. A beneficiary with a cognitive disability may not have the ability to review and understand financial statements and therefore would be unable to provide informed consent to the settlement of a trustee's account. While a trust could be drafted to allow a third party (like a parent or guardian) to review and approve a trustee's accounts, courts tend to frown on informal settlements by guardians,⁷⁶ especially in cases where the guardian has a conflict (such as when the parent-guardian resides in a home owned by and financially supported by the trust).
2. Evidence that a fiduciary has provided all beneficiaries with copies of financial statements, tax returns and other trust activity will not preclude a later challenge in a proceeding for settlement of the fiduciary's account, especially where a beneficiary has a cognitive disability.⁷⁷
3. Relying solely on the delivery of financial statements presents even greater risk for the trustee of a first party supplemental needs trust, where the Medicaid program is entitled to be repaid upon the death of the beneficiary and is thus an interested party in any proceeding for settlement of the trustee's accounts. Financial statements reviewed as part of a Medicaid application or redetermination do not bind the agency and do not preclude a later proceeding to recover incorrectly paid Medicaid.⁷⁸ Nor do they address the prospect that the trust remainder may not be sufficient to satisfy the Medicaid claim upon the beneficiary's death to recoup correctly paid Medicaid. Medicaid program representatives insist on formal judicial settlement for a fiduciary to be released when a trust is terminating, payment of the Medicaid recovery is due, and the recovery cannot be fully satisfied by the trust remainder.
4. Information presented on complex financial statements can be confusing and difficult to understand. If the information is not clear and complete, a release based on that information may be unenforceable.⁷⁹

⁷⁶ 7 Warren's Heaton on Surrogate's Court Practice § 94.02(2)(a) (2019).

⁷⁷ In determining whether an informal account by a trustee is adequate, "the court must consider that [the beneficiary] is an adult under no disability." *Matter of Spacek*, *supra* n. 45 at 8.

⁷⁸ N.Y. Soc. Serv. L 366(2)(b)(2)(v); *Oxenhorn v. Fleet Trust Co.*, 94 NY2d 110 (1999).

⁷⁹ *Matter of Spacek*, *supra* n. 45.

4. Traditional accountings do not address the unique responsibilities associated with SNT administration.

Some trustees provide informal accountings to their beneficiaries on an annual or other periodic basis. The format and level of detail vary, but these informal accountings rarely identify and address issues that would be the subject of inquiry by the agencies administering the Medicaid or SSI programs.⁸⁰

Accountings prepared by corporate trustees frequently combine reimbursements for various items into a single 'discretionary distribution' rather than separate them by category. Thus, a reimbursement to a family member might include items which would impact SSI (such as groceries) as well as items which would not (such as a cell phone bill). Supplemental needs trust accountings should segregate distributions by the type of expense and use the informational schedules to identify distributions which may impact public benefits.

Similarly, these informal accountings may not identify transactions which provide a derivative benefit to third parties or may not address those transactions in the explanatory schedules.⁸¹

Consider a trustee who, after consulting with a beneficiary and her guardian, decides to use funds in an SNT to pay rent so that the beneficiary and her guardian can move into a decent apartment. That payment would be reflected on the informal accounting. An accompanying note in the explanatory schedule would confirm that the guardian is paying his portion of the rent, that payment from the trust is being made with the understanding that there will be an offset to the beneficiary's monthly SSI payment, and that the beneficiary and her guardian have reported the ongoing payment to the SSI program in anticipation of the adjustment. By doing so, the informal accounting will reflect that the trustee has made an *informed* decision and that the trustee has *considered the impact of the distribution on government benefits*.

5. Filing an informal accounting is not the same as petitioning for judicial settlement.

When an SNT is funded by court order, the order will often require that an annual accounting be filed with the court for review by an examiner or fiduciary clerk. Accounting format varies, and the review is more of a financial reconciliation to ensure that the accounts balance and that distributions were made in compliance with any restrictions or limitations that may have been imposed by the court.

⁸⁰ Lewis, Kristen M., Esq. and Lowder, Janet L., Esq., *SNT Beneficiaries on the Move: Issues with SNT Portability*, at p. 7 (Stetson University College of Law 2017 National Conference on Special Needs Planning and Special Needs Trusts).

⁸¹ See recent revisions to the Social Security Administration's Program Operations Manual System ("POMS") SI 01120.200–203, effective April 30, 2018, which adopted the "primary benefit" test for SNT distributions. New York has utilized the primary benefit test since 1996. See OBRA 93 Provisions on Transfers and Trusts, NYS Department of Social Services Administrative Directive, 96 ADM 8 (March 1996), at (IV)(7)(b)(ii).

This administrative review does not formally settle the trustee's accounting.⁸² As such, these *ex parte* submissions do not protect a trustee from later challenge by a remainder beneficiary or, in the case of a first party SNT, by the Medicaid program.⁸³ In order for the trustee to be formally released from any further liability for information contained in the accounting it would have to petition for judicial settlement with service on all interested parties.⁸⁴

This lack of a binding determination presents a particular risk for trustees of first party supplemental needs trusts. Eventually these trusts will terminate, and the trustee will need to formally account, a process which includes the determination of the Medicaid program's repayment amount. Increasingly, state Medicaid programs are hiring national for-profit entities known as "Medicaid Recovery Audit Contractors" to pursue their recovery rights.⁸⁵ These companies have their own proprietary procedure for review and interpretation of the responsibilities of the trustee of a supplemental needs trust and would not be bound by informal filings with a state court.

Finally, the scope of a trustee's responsibility to the Medicaid program upon the death of the beneficiary remains unclear. The Social Security Administration takes the position that the trustee of a trust where the beneficiary is receiving an SSI benefit is responsible to ascertain and resolve repayment obligations to every state in which a beneficiary has ever resided,⁸⁶ although the language of the federal supplemental needs trust statute contains no such affirmative obligation. If a deceased beneficiary lived in a number of states, will service on the Medicaid program representative in the state where the beneficiary last received Medicaid be sufficient to bind the Medicaid program? There are apparently no reported decisions on this issue.⁸⁷

6. Annual proceedings for advice and direction or judicial settlement would be impractical and cost ineffective.

The aspects of SNT administration highlighted here – communication challenges, unfamiliar government benefit programs, and the inability to informally settle accounts – present unique risks for SNT trustees.

Given these risks, a prudent trustee might be inclined to seek judicial approval of its actions on a regular – and perhaps an annual – basis. The trustee could petition for

⁸² In some counties the examiner's approval will be accompanied by an order acknowledging its submission and approving the examiner's fee, but the informational accounting is still an *ex parte* submission and will not have the same legal effect as an order obtained in a proceeding for judicial settlement of the trustee's accounts.

⁸³ *Matter of Salvati*, 90 A.D.3d 406 (1st Dep't 2011).

⁸⁴ *Comm'r. of the NYC Dept of Social Services v. New York Presbyterian Hospital, Chi Young Lee and BNY Mellon, N.A.*, 47 Misc. 3d 1204(A) (Sup. Ct., N.Y. Co. 2015).

⁸⁵ Lewis and Lowder, *supra* n. 80. See also <http://hms.com/special-needs-trust-recovery-services/>.

⁸⁶ POMS SI 01120.203(B)(10).

⁸⁷ The POMS are not statute or regulation, and the agency's interpretation of this statutory reimbursement requirement should be given limited weight in a state court proceeding for the settlement of a trustee's accounts.

judicial settlement of its accounting or could seek "advice and direction" on a proposed distribution plan. Both proceedings present risks of their own, and neither approach – if undertaken annually - would be cost effective.

A trustee could present a formal accounting for judicial settlement on an annual basis.⁸⁸ Where the beneficiary has a cognitive disability, and regardless of whether a property guardian has been appointed, most courts will appoint a guardian *ad litem*, especially where a court-appointed guardian resides with the beneficiary and has indirectly benefitted from the use of trust funds. Some guardians *ad litem* are attorneys with significant experience in special needs planning and disability benefits, but many are not. Inexperienced guardians *ad litem* can complicate a proceeding for settlement.

Because the Medicaid program is considered to have a remainder interest in a first party supplemental needs trust,⁸⁹ the Medicaid program representative will be a necessary party to the proceeding for judicial settlement. The Medicaid program representative will then have an unfettered opportunity to challenge discretionary distributions appearing on the accounting, focusing on distributions which would have an impact on "benefit eligibility"⁹⁰ or reduce the amount available for post-mortem recovery.

Alternatively, a trustee could seek "advice and direction" on an annual basis: court approval for a distribution plan developed in conjunction with the beneficiary (or the beneficiary's guardian), a care manager, or others involved in the beneficiary's life. By having a distribution plan approved in advance, the trustee would be insulated from challenge so long as a later accounting showed that distributions were made in compliance with the court approved plan.

Yet courts regularly refuse to entertain petitions for advice and direction when a matter is considered to be within the discretion of a trustee or guardian.⁹¹ Moreover, this approach would require a return to court whenever a plan needed to be modified based on changes in health, household composition or other factors that are impossible to predict with certainty. And as with a petition for judicial settlement of the trustee's accounting, the Medicaid agency will be a necessary party to the proceeding and will have standing to dispute the proposed plan of care or the budgeted amount, or otherwise seek to limit distributions and increase the amount available to satisfy the Medicaid program's recovery upon the beneficiary's death.⁹²

⁸⁸ SCPA 2208(3)(b).

⁸⁹ N.Y. Soc. Serv. L. § 366(2)(b)(2)(v).

⁹⁰ See *Matter of Tinsmon (Lasher)*, *supra* n. 29, where a representative from New York's Medicaid program argued against an otherwise permissible distribution from an SNT based on its interpretation of the SSI program rules, a program that the agency had no authority to administer, and no particular expertise to interpret. Both the lower court and the appellate court disposed of the agency's arguments in short order, but the trustee still had to spend the time and money in litigation.

⁹¹ *In re Hagadorn*, 176 Misc. 233 (Sup. Ct. New York County 1941); *In re Meenan*, 46 NYS2d 282 (Sur. Ct. Westchester County 1944); *In Re William M. Kline Revocable Trust*, *supra* n. 54.

⁹² *Matter of Tinsmon (Lasher)*, *supra* n. 29.

7. Recommendation:

In order to manage and mitigate risk, the trustee should take the following steps:

1. The trustee should prepare an informal accounting of trust activity on an annual basis, and provide copies of the accounting to the beneficiary with the disability (if competent, or to the court appointed guardian or agent under power of attorney if not) and to the Medicaid program representative if the trust is a first party SNT.⁹³ If the beneficiary is a minor, the beneficiary's parents should also receive a copy.

The informal accounting should clearly delineate distributions which would have an impact on benefit eligibility, or which provide a derivative benefit to third parties, and should include clarifying information in the explanatory schedules as appropriate.

Finally, the informal accounting should be prepared in the same format that would be required in a proceeding for judicial settlement so that the trustee can move quickly to have its accounts settled if any party receiving a copy raises an issue. This is especially important for first party supplemental needs trusts where the Medicaid program will be a necessary party to any settlement proceeding.

2. On a periodic basis, the trustee's accounts should be judicially settled. Even if a trustee is providing comprehensive informal accountings on an annual basis to all beneficiaries and none of the beneficiaries raise an issue, the trustee should nonetheless petition for judicial settlement after a number of years in order to wipe the slate clean. Frequency will depend on a number of factors. If a trustee is making regular and significant distributions from a well-funded trust, it might petition for judicial settlement every few years. If the trust is modestly funded and relatively inactive, it might petition less frequently.

This recommendation is not limited to SNT trustees. Circumstances which can complicate the settlement of a trustee's accounting (whether informally by agreement or by court order) are familiar to attorneys who represent trustees in contested accounting proceedings. Older financial records are lost or unavailable, a common occurrence in an era of bank consolidation. Trust officers retire, taking with them the first-hand knowledge of a beneficiary's circumstances and the basis for certain discretionary distributions. Relationships with beneficiaries may sour over time, increasing the likelihood of objections.

For trustees of SNTs, there are additional variables and uncertainties. Government benefit program rules change over time, and a distribution that might have had no impact on a particular benefit under a prior policy may now result in a penalty. New programs might emerge which provide funding for services that the trustee has been paying for with trust funds for many years. Finally, attorneys who represent the Medicaid program in proceedings for judicial settlement also retire, and their replacements may take a much

⁹³ In our first party supplemental needs trust practice we provide copies of annual accountings to the Medicaid program representatives, and to other remainder beneficiaries when possible and practical.

more adversarial approach in settlement proceedings. Periodically seeking judicial settlement puts all parties on notice – the beneficiary with the disability, the Medicaid program (for first party SNTs), and the remainder beneficiaries – and requires them to present their objections for review by the court.

3. For significant transactions or transactions which would clearly result in a derivative benefit to someone other than the beneficiary, the trustee should seek prior court approval. In New York, this is typically done through a petition for advice and direction.

8. Acknowledging the deviation from standard practice.

This approach – comprehensive informal annual accountings, regular petitions for judicial settlement, and periodic applications for court approval - is antithetical to traditional estate planning, where attorneys try to limit administrative expense and judicial oversight when drafting trusts, and where trustees try to avoid interaction with the courts. Disability advocates may be concerned over the financial impact of this approach on individuals with disabilities who have trusts of more limited amounts. We understand these concerns.

On the other hand, attorneys and other advocates do a disservice to SNT beneficiaries and trustees when they fail to explain the level of exposure faced by the trustee of an SNT (especially a first party SNT), or when they try to draft around the formalities associated with trust administration. If all trust beneficiaries are competent and capable of self-advocacy, estate planners can draft documents to minimize administrative responsibilities and the associated costs. If a trustee cuts corners in keeping records, providing financial statements, or filing tax returns, the beneficiaries may decide to look the other way rather than endure the time and expense of a formal accounting.

But such informal settlement is typically not an option for SNTs, especially first party SNTs where the Medicaid program is one of the interested parties. Medicaid's priorities are contrary to those of the beneficiary with the disability and the remainder beneficiaries. The less the trustee spends during the beneficiary's life, the more that this statutory creditor will recover upon the beneficiary's death.

Informal accountings prepared and presented on an annual basis create a record of full disclosure which may serve as a basis to defend against objections in a proceeding for judicial settlement,⁹⁴ periodic judicial settlement limits the trustee's ongoing risk, and petitions for advice and direction protect future distributions from later challenge.

⁹⁴ In New York, the failure to object may be considered 'ratification' and serve as a basis for a motion to dismiss the objections of an informed remainderman. *Rajamin v. Deutsche Bank Nat'l Trust Co.*, 757 F.3d 79 (2d. Cir. 2014). Would the Medicaid program be similarly bound? One might argue that a government agency cannot be estopped. See *Oxenhorn v. Fleet*, *supra* n. 78. This position fails to recognize that in New York, the Medicaid program is named as a beneficiary by statute (N.Y. Social Serv. L. § 366(2)(b)(2)(v)). In a state court proceeding for settlement of a trustee's accounts, the Medicaid program's interest should be no greater and no less than that of any other remainder beneficiary.

V. Matter of J.P. Morgan and Matter of Liranzo revisited

Two New York decisions which received significant attention within the fiduciary community involved surcharge (or the threat of surcharge) against a trustee for failing to fulfill its responsibilities under the terms of a supplemental needs trust – one for spending too little, the other for spending too much. Here we revisit those decisions to see how the courts approached the standard of review, and to determine whether implementation of some of the procedural recommendations outlined in this article might have led to a different result.

A. Matter of JP Morgan

In *Matter of JP Morgan*,⁹⁵ the Court criticized the trustee of a well-funded third party SNT for collecting commissions while trust funds sat dormant. The beneficiary lived at a residential school for individuals with disabilities in upstate New York. The beneficiary's mother funded the trust upon her death in 2005, appointing her attorney and a bank as co-trustees. The attorney later petitioned to become the beneficiary's guardian, and in connection with that proceeding the Court directed the trustees to petition for judicial settlement of their accounts.

The Court learned that in the five years subsequent to the mother's death, no distributions were made for the beneficiary. Neither co-trustee visited the beneficiary nor contacted staff at the school to inquire of his needs. Neither co-trustee notified school staff of the existence of the trust. The bank co-trustee testified that it lacked the "institutional capacity to ascertain or meet the needs of this severely disabled, institutionalized young man."⁹⁶ Both co-trustees took their commissions.

1. The co-trustees satisfied the basic obligations of fiduciary conduct.

The decision suggests that the trustees satisfied their traditional fiduciary responsibilities: they invested the funds in the trust, filed tax returns, and were able to fully account when directed by the Court.⁹⁷

2. The co-trustees failed to establish a protocol for communication or a plan to assess and review programs and services.

Satisfying the basic responsibilities of fiduciary conduct was not enough. In the words of the Court:

It was not sufficient for the trustees merely to prudently invest the trust corpus and to safeguard its assets. The trustees here were affirmatively charged with applying trust assets to [the beneficiary's] benefit and [were] given the discretionary power to apply additional income to [the beneficiary's] service providers. Both case law

⁹⁵ *Matter of JP Morgan*, *supra* n. 8.

⁹⁶ *Id.* at 370.

⁹⁷ While the trustees were able to account for funds held in the SNT, the Court questioned the accuracy of the accounting for the prior estate and the initial SNT funding amount. *Id.* at 379.

and basic principles of trust administration and fiduciary obligation require the trustees to take appropriate steps to keep abreast of [the beneficiary's] condition, needs, and quality of life, and to utilize trust assets for his actual benefit.⁹⁸

The judge directed the trustees to hire a care manager to investigate, report and facilitate distributions for the beneficiary. The care manager visited the beneficiary, attended team meetings, provided the co-trustees with quarterly reports, made purchases, and served as an intermediary between residential staff and the trustees.⁹⁹ The care manager made a number of recommendations, including a consultation with a "non-Medicaid neurologist" who recommended medication that was not covered by Medicaid but had fewer side effects, the purchase of computer equipment and software for adaptive communication, recreational equipment, and gift certificates for local merchants so that the beneficiary could experience the outside community. The beneficiary made "extraordinary - and heartwarming – progress"¹⁰⁰ as a result of these expenditures.

3. The drafting attorney attempted to limit the trustees' obligation to account.

The attorney co-trustee drafted the SNT and apparently tried to limit the trustees' obligation to account to its beneficiaries, something which the Court held:

violates public policy and cannot be enforced, where, as here, the beneficiary is a person under a disability, and no one is protecting the beneficiary's interests.¹⁰¹

The decision does not provide any insight into why the drafting attorney tried to limit the accounting requirement. The provision might have been taken from a standard discretionary trust and intended to limit administrative costs. Regardless, had the trust included a provision requiring the trustees to prepare an informal accounting on an annual basis, it is likely that a representative of the residential program would have become aware of the trust and could have provided the trustees with information on the beneficiary's needs.

4. The Court clearly articulated a standard of review.

The Court held that the trustees' actions – or, more specifically, their inaction – constituted an abuse of discretion:

⁹⁸ *Id.*

⁹⁹ *Id.* at 371. It is important to note that the beneficiary resided in a Medicaid funded residential program with round the clock staffing and related support. The Court nonetheless directed the co-trustees to retain and pay a private care manager to monitor those supports, and in some cases provide services that would otherwise have been provided by Medicaid-funded staff, such as scheduling doctors' visits or consulting with specialists. The case illustrates the difference between the baseline or "floor" provided by public benefit programs and the optimal level of services and support that might be available through the proactive expenditure of funds from an SNT. See *Footte v. Albany Med. Ctr. Hosp.*, 71 A.D. 3d 25 (3d Dep't 2009), *aff'd*, 16 N.Y. 3d 211 (2011).

¹⁰⁰ *Matter of J.P. Morgan*, *supra* n. 8 at 370.

¹⁰¹ *Id.* at 377, citing *Matter of Malasky*, 290 A.D. 2d 631 (3d Dept 2002), and *Matter of Shore*, 19 Misc. 3d 663 (Sur. Ct., N.Y. Ct. 2008).

Courts will intervene not only when the trustee behaves recklessly, but also when the trustee fails to exercise judgment altogether ("even where a trustee has discretion whether or not to make any payments to a particular beneficiary, the court will interpose if the trustee, arbitrarily or without knowledge of or inquiry into relevant circumstances, fails to exercise the discretion").¹⁰²

In *Matter of JP Morgan*, the trustees' mistake was not necessarily the failure to make expenditures for the beneficiary's benefit. Rather, the trustees failed to promptly establish a protocol for communicating with the beneficiary's staff and assessing his needs. Had the trustees retained the private care manager promptly upon being appointed, they would have had the information needed to enhance his quality of life by supplementing the care and support he was receiving at the residential school.

Alternatively, the care manager's report might have reflected that the beneficiary was thriving, that the beneficiary's mother (who died just a few years earlier) had already purchased many items to enhance her son's quality of life, and that - at the moment - the beneficiary needed for nothing. On these facts the accounting might have looked substantially the same, but the trustee would have been able to document that it met all of its traditional fiduciary obligations, and it would also be able to show that its decision not to spend funds over the past few years was not an abuse of discretion, but rather an *informed decision* made after a comprehensive review.

B. Matter of Liranzo

In *Matter of Liranzo*,¹⁰³ a bank serving as corporate trustee of a first party supplemental needs trust funded with litigation proceeds sought to settle its account and terminate the trust. The trust was initially funded with just over \$420,000. Six years later, the trust had approximately \$3,200 remaining. The accounting showed that the largest expenditures were for private caregivers and taxi service for the beneficiary.

1. The trustee failed to satisfy some basic obligations of fiduciary conduct.

There did not appear to be any credible analysis of the long-term financial impact of the level of spending undertaken by the trustee.¹⁰⁴ Additionally, the trustee authorized "each and every discretionary disbursement requested by the infant plaintiff's mother"¹⁰⁵ rather than exercising independent judgment on the propriety of those distributions.

2. The trustee maintained communication with the beneficiary's family member.

¹⁰² *Id.* at 377, quoting Restatement (Third) of Trusts, § 50, comment b.

¹⁰³ *Liranzo*, *supra* n. 9.

¹⁰⁴ *Id.* at 4.

¹⁰⁵ *Id.* at 5.

In *Matter of Liranzo* there was an involved parent – the beneficiary’s mother – and the trustee was in regular communication with her.¹⁰⁶

3. The trustee did not adequately assess the availability of Medicaid funded services.

Regarding the private caregivers, a representative from the bank trustee testified that an "advocate for the [beneficiary]"¹⁰⁷ communicated with the local Medicaid agency about the availability of Medicaid funded staff and informed the trustee that Medicaid funded aides were unavailable. The trustee also testified that it "consulted with [the beneficiary's mother] and social workers that concluded private caregivers were in the best interest of [the beneficiary]."¹⁰⁸

While there were a number of hearings and conferences, the decision does not reference testimony from the "advocate for the [beneficiary]" or any of the social workers upon whom the trustee relied in deciding to pay privately for caregivers. The decision suggests that the trustee communicated primarily with the mother and did not retain its own professional to corroborate the information that the mother was providing.

Similarly, the Court held that the trustee should have "further investigated" the mother's representation that riding in a taxi helped ease the beneficiary's stress before agreeing to spend more than \$50,000 on the expense over a six-year period.¹⁰⁹

4. The Court did not clearly articulate a standard of review.

In Part V of this article we reviewed the various explanations that the Court used in finding that the trustee breached its fiduciary duty to the beneficiary. The decision begins with the statement that the trustee breached its fiduciary duty by "failing to make decisions based on the long-term needs of the beneficiary that would extend the life of the Trust for as long as possible."

In surcharging the trustee for payments made to the taxi service, the Court found that such payments "do not appear to be a responsible use of Trust fund monies consistent with prolonging the life of the Trust."

Later in the decision the Court criticizes the trustee for making distributions which "could have either been avoided or were unreasonable" or reflected a failure to administer the trust in the "sole interests of the beneficiary."

At no point did the Court clearly articulate the standard it was applying in assessing the trustee's conduct. As a result, the decision does not provide any practical guidance beyond the specific (and admittedly concerning) facts of the case.

5. An abuse of discretion analysis would provide the same result with better guidance.

¹⁰⁶ The decision does not say whether the mother was also a court appointed guardian.

¹⁰⁷ *Liranzo*, *supra* n. 9 at 5.

¹⁰⁸ *Id.* at 6.

¹⁰⁹ *Id.* at 7.

If the Court applied an abuse of discretion analysis, it could have reached the same conclusion, but with better guidance for SNT trustees.

The trustee's failure to consider the long term impact of paying for private caregivers and taxi rides would support a finding that it abused its discretion under the basic rules of fiduciary conduct which require a trustee to balance the immediate needs of the beneficiary with probable future needs.¹¹⁰

The trustee's blind reliance on representations made by the beneficiary's mother would support a finding that it abused its discretion by failing to independently investigate its beneficiary's needs.¹¹¹

The trustee's failure to thoroughly investigate Medicaid funded alternatives would support a finding that it abused its discretion by failing to follow the terms of the governing document, which require consideration of public benefits and services before expending trust funds.¹¹²

6. The trustee's biggest mistake was the failure to promptly obtain an independent assessment of its beneficiary's needs.

Upon being appointed, the trustee should have promptly investigated the availability of Medicaid-funded goods and services and determined whether they were adequate, or whether they should be supplemented by expenditures from the trust. Had the trustee retained a private care manager to conduct an independent assessment, it might have learned that there were indeed Medicaid funded home care programs that would have provided aides for its beneficiary, and it might have learned of other, less expensive but equally effective therapeutic alternatives to riding in a taxi to calm the nerves.

Alternatively, the trustee might have decided to spend money in the same way. For example, the care manager's report might have disclosed that the beneficiary was approved for Medicaid funded staff but was unable to find aides willing to work at the Medicaid payment rate. The report might have disclosed that the beneficiary had unique and complicated behavioral issues, and that the privately paid aide (who did not accept Medicaid) was the only one capable of managing those behaviors. The report might have disclosed that taxi rides did indeed calm the beneficiary, but without the debilitating side effects caused by the anti-anxiety medication he would otherwise have to take. Finally, the report might have disclosed that the beneficiary had a shortened life expectancy and the mother wanted him to have the best quality of life possible in his final years.

Based on the care manager's report, the beneficiary's limited life expectancy, and the support of the mother, the decision to aggressively apply income and principal to pay for

¹¹⁰ *Estate of T. Harry Glick*, *supra* n. 18.

¹¹¹ *Matter of Hammerschlag*, *supra* n. 48.

¹¹² New York Estates Powers & Trusts Law (EPTL) 11-1.1(a)(2).

private caregivers and taxi services rather than rely on Medicaid funded supports would not necessarily be an abuse of discretion, notwithstanding the fact that it depleted the trust in a short period of time,¹¹³ and notwithstanding the fact that the Court might have made a different decision on the same set of facts.

7. A petition for advice and direction would have insulated the trustee from liability.

Even with a comprehensive assessment from a private care manager and the support of a parent, a prudent trustee should be concerned about spending so much in such a short period of time. To mitigate risk, the trustee could seek prior court approval of its proposed distribution plan.

A court might refuse to consider the application, as it is essentially a request to substitute the court's judgement for that of a trustee with full discretion under the terms of the governing document. But in such a case, the trustee would have a record of its attempt to secure court approval. While not binding in a subsequent proceeding for settlement of its accounts, it would buttress the argument that the trustee's exercise of discretion was encouraged by the court and should be upheld over later objections.

VI. Conclusion

The need for professional advocates for individuals with disabilities will continue to grow with each passing year. With aging parents increasingly unable to provide support to their sons and daughters with disabilities, and with disability service providers stretched thin by cuts in government funding, professional caregivers and fiduciaries will be asked to take on greater responsibility in serving the needs of those who cannot care for themselves.

In recent years many otherwise capable financial institutions have declined to administer supplemental needs trusts, in large part because of the uncertainty over how their conduct will be measured after the fact. Cases like *Matter of JP Morgan* and *Matter of Liranzo* reinforce these concerns.

The well-established body of law governing discretionary trusts is more than capable of accommodating the unique aspects of supplemental needs trust administration. The failure to apply the abuse of discretion standard has discouraged the development of commonly accepted "best practices" which, if followed, would better serve beneficiaries of supplemental needs trusts, and help insulate trustees from the risks associated with this type of administration.

¹¹³ New York's supplemental needs trust statute makes clear that the trustee may exhaust trust principal "even to the extent of the whole" for the benefit of the beneficiary. EPTL 7-1.12(e)(1).
