

The Sole Benefit Rule and Administration of Pooled Special Needs Trusts

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Program Overview

This session examines the Sole Benefit Rule under federal Medicaid law and its application to the administration of pooled special needs trusts. Attendees will explore how trustees can navigate complex distribution decisions while maintaining compliance with 42 U.S.C. §1396p(d)(4)(C) and POMS SI 01120.203. The presentation provides both the legal foundation and practical guidance for trustees, attorneys, and fiduciaries.

Learning Objectives

- Understand the legislative intent and policy rationale behind the Sole Benefit Rule.
- Apply the POMS standards for permissible and impermissible expenditures.
- Evaluate common 'red flag' transactions that risk disqualification.
- Implement administrative best practices and documentation strategies.

Federal Framework

Under federal law, trusts established for individuals with disabilities may be exempt from Medicaid resource consideration if they meet statutory criteria. A trust that is established for a disabled individual is not considered an asset or resource for Medicaid purposes if the trust includes provisions that require the trust assets to be spent only to supplement, rather

than supplant or replace, government benefits, and has provisions that require it to repay the state Medicaid agency after the trust terminates. Such trusts are meant to provide goods and services above and beyond what Medicaid will provide—and which will enhance the disabled beneficiary’s life.

Federal law specifically exempts “pooled” trusts administered by non-profit organizations. A pooled trust can be funded with a disabled individual’s assets and/or the assets of the person’s parent, grandparent, a legal guardian, or a court. A pooled trust does not need to be established before the individual reaches age 65, a requirement that applies to other exempt trusts permitted under federal law. Indeed, a pooled trust is the only method under current law for a disabled individual over the age of 65 to place their own assets without disqualifying them from receiving Medicaid benefits.

Specifically, a pooled trust under 42 U.S.C. §1396p(d)(4)(C) must be administered by a nonprofit association, maintain separate accounts for each beneficiary, and include payback or retention provisions. A key compliance requirement is that each sub-account be established for the *sole benefit* of the disabled individual.

Legislative Intent and Policy

Congress enacted the Omnibus Budget Reconciliation Act of 1993 (OBRA ’93) to protect assets belonging to individuals with disabilities while ensuring Medicaid resources are used appropriately. The Sole Benefit Rule was created to ensure that trust assets enhance a beneficiary’s quality of life without providing windfalls to others. The rule preserves eligibility for public benefits while allowing beneficiaries access to supplemental goods and services.

Overview of the Sole Benefit Rule

To be considered an exempt under pooled trust rules, the individual trust account (or the “sub-account”) must be established for the sole benefit of the disabled individual. According to POMS, which state Medicaid agencies use as a guide on federal pooled trust requirements, a trust is considered to be established for the sole benefit of an individual “if the trust benefits no one but that individual, whether at the time the trust is established or at any time for the remainder of the individual’s life” A trust that allows the trust assets or income to be paid to or for the benefit of any individual or entity other than the beneficiary is not established for the sole benefit of the disabled individual.

The Sole Benefit Rule requires that all disbursements from a pooled trust be made for the sole benefit of the disabled beneficiary. According to POMS SI 01120.203, a trust is not considered for the sole benefit of an individual if it allows assets to be used for anyone other than the beneficiary during their lifetime. However, incidental or collateral benefits do not necessarily constitute violations.

Application of *Lewis v. Alexander* to the Sole Benefit Rule

The *Lewis v. Alexander* decision (3d Cir. 2012) clarified that states may not impose additional substantive requirements on pooled special needs trusts beyond those enumerated in 42 U.S.C. § 1396p(d)(4). This holding directly impacts how states interpret and enforce the Sole Benefit Rule.

Federal law requires that expenditures from a pooled trust be for the sole benefit of the disabled beneficiary. However, some states had attempted to restrict that principle by

adding limitations such as “reasonable relationship to the beneficiary’s needs” or prohibiting certain expenditures that incidentally benefit others.

The Third Circuit rejected these added state restrictions, finding them preempted by federal law. The court held that:

- The federal statute’s list of criteria for pooled trusts is exclusive, leaving no room for state modification.
- The “sole benefit” standard must be interpreted under federal law and SSA POMS guidance (SI 01120.201 and SI 01120.203), not by varying state definitions.
- States may monitor trusts and enforce compliance, but they cannot redefine “sole benefit” or add “reasonableness” or “special needs” requirements.

The practical implications of *Lewis v. Alexander* include:

- Trustees and fiduciaries should evaluate disbursements using the federal definition of “sole benefit,” which allows incidental benefits to others if the primary purpose is for the beneficiary.
- Attorneys can rely on *Lewis* to challenge state attempts to deny eligibility or impose penalties based on non-federal interpretations.
- This decision reinforces that uniform federal standards govern the creation and administration of pooled special needs trusts nationwide.

Exceptions to the Sole Benefit Rule

It is important to understand the exceptions to the sole benefit rule. Some of the major exceptions to the sole benefit rule, as outlined in POMS, are as follows:

- 1) Payments to third parties that provide goods or services to the beneficiary (e.g., purchasing a home or television).
 - a. A trustee can make a payment to a third-party if the *primary* benefit goes to the trust beneficiary. According to POMS, “you should not read this so strictly as to prevent any collateral benefit to anyone else. For example, if the trust buys a house for the beneficiary to live in, that does not mean that no one else can live there, or if the trust purchases a television, that no one else can watch it. On the other hand, it would violate the sole benefit rule if the trust purchased a car for the beneficiary’s grandchild to take the beneficiary to their doctor’s appointments twice a month, but the grandchild was also driving it to work every day.”
 - b. It is acceptable for trust assets to pay a family member who is providing services to the trust beneficiary, as long as the payments are reasonable and customary for similar services being provided in the geographic area. The fact that the person is a family member does not change the analysis.
 - c. Trust payment for companion expenses can be a valid expense paid to a family member. According to POMS, “[f]amily members may normally

do some of these things without compensation, but that does not prohibit the trust from paying for these services.”

- d. Incidental expenses are acceptable. An example of an acceptable incidental expense is if a companion takes the trust beneficiary to a museum. The trust can pay for the admission for the companion to the museum, as this is part of the cost of providing the service.

2) Payments to of travel expenses (transportation, lodging, and food) for a third-party to accompany the trust beneficiary.

- a. A trust may pay for the travel expenses of a third-party if the service or assistance of the third-party is “necessary to permit the trust beneficiary to travel.” For example, a minor child cannot travel unaccompanied and requires an adult to travel with them. Payment for the adult to travel with the minor child who is the trust beneficiary is not prohibited.
- b. A “reasonableness test” is used for evaluating the number of people the trust is paying to accompany the beneficiary. It would violate the sole benefit rule if the trust paid for other individuals who are not providing services or assistance *necessary for the beneficiary to travel*.
- c. Trust payments for other children in the family to travel along with a disabled minor child who is the trust beneficiary is prohibited by the sole benefit rule.

3) Payments of third-party travel expenses to visit a trust beneficiary.

- a. Travel for a service provider (including a family member) to oversee the trust beneficiary’s living arrangements when the beneficiary lives in a

long-term care facility or other supported living arrangement is acceptable under the sole benefit rule.

- b. Travel for a trustee or trust advisor (including a family member) to exercise their fiduciary duties or to ensure the well-being of the beneficiary is acceptable under the sole benefit rule.

- 4) Trustee and professional fees for management, investment, and legal services rendered on behalf of the trust.

- a. The trust may pay for reasonable compensation for managing the trustee(s) and reasonable costs associated with investment, legal, or other services rendered on behalf of the individual regarding the trust.

Case Studies and Hypotheticals

For each scenario, consider: Does this violate the Sole Benefit Rule? Why or why not?

- Purchase of a home titled to the trust, where family members also reside.
- Payment of above-market caregiver compensation to a sibling.
- Trust-funded family vacation that provides mixed benefit.
- Airfare for family visits versus fiduciary monitoring visits.

Trustee Guidance and Best Practices

- Maintain documentation for each disbursement decision, including invoices and notes on benefit to the beneficiary.
- Execute written service agreements for family caregivers or service providers.

- Perform annual reviews of the trust’s purpose, distributions, and continued compliance with Medicaid eligibility.
- Consult with legal counsel or benefits specialists before making discretionary expenditures.
- Train fiduciary and administrative staff on current SSA and DHS interpretations of the rule.

Common Compliance Pitfalls

- Paying for goods or services already covered by governmental programs.
- Depositing assets received from government entities into the pooled trust.
- Commingling assets between beneficiaries or with the nonprofit’s operational funds.
- Failing to document the direct benefit to the trust beneficiary.

Key Legal Authorities and References

- 42 U.S.C. §1396p(d)(4)(A)–(C)
- Omnibus Budget Reconciliation Act of 1993 (OBRA ’93), Pub. L. No. 103-66, §13611
- SSA POMS SI 01120.203 – Trusts Established under §1917(d)(4)(C)
- SSA POMS SI 01120.201 – Trusts and Sole Benefit Requirements
- CMS State Medicaid Manual §§ 3257-3259
- *Lewis v. Alexander*, 685 F.3d 325 (3d Cir. 2012)
- *Pfoser v. Harpstead*, 953 N.W.2d 507 (Minn. 2021)

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