



“Special Needs Trusts in Pennsylvania”

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Special Needs Trusts (SNT) are designed to permit financial resources to remain available to assist an individual with disabilities who receives, or may receive in the future, Medical Assistance (also known as Medicaid or MA) and/or Supplemental Security Income (SSI) benefits, and/or Mental Health and Intellectual Disability (MH/ID) benefits.

There are three types of SNTs, each of which is defined by how it is funded: 1) a “Third Party Funded SNT” involves funding by a third party other than the beneficiary; 2) a “Self-Funded SNT” involves funding with the beneficiary’s own monies; and 3) a “Pooled SNT” involves individual accounts funding a common fund with a non-profit fiduciary, similar to a mutual fund program.

SNTs which are properly drafted and administered, protect a person with disabilities who receives MA, SSI and MH/ID benefits from disqualification for these benefits by the Department of Public Welfare or the Social Security Administration for MA, SSI or MH/ID benefits. Under present law, SNTs may be created to completely avoid such disqualification. Third Party Funded SNTs cannot be invaded by public authorities so long as the SNT clearly reflects the intent of the Settlor that corpus of the SNT not be available as a “resource” with regard to public benefits. Federal law with respect to Self-Funded SNTs, explicitly permits the creation and maintenance of lifetime Trusts for disabled MA recipients with their own funds. The Pennsylvania Rules of Civil Procedure expressly permit the use of SNTs in resolving civil litigation.

Third Party Funded Special Needs Trusts

When establishing a Third Party Funded SNT it must be clearly stated that 1) it is the intent of the settlor to supplement and not supplant public benefits and that such benefits be considered prior to distribution of any SNT income or principal; 2) the SNT is irrevocable; and 3) the trustee has total, absolute and unfettered discretion to pay, or refuse to pay, income or principal from the SNT to the disabled beneficiary. Never instruct the trustee to make periodic (e.g., monthly) payments, as all payments should be discretionary. While expenditures may be made for food or shelter it is critical to do so after consultation with your trust advisor to comply with MA and SSI rules.

Self-Funded Special Needs Trusts

Self-Funded SNTs are permitted under 1993 Amendments to the Social Security Act to allow SNTs where the beneficiary’s own monies are used. The applicable rules require that 1) the SNT be created irrevocably for the sole benefit of a disabled individual under age 65; 2) the SNT be created by the beneficiary’s parent, grandparent, guardian or a court; 3) the state agency which operates the Medicaid program will be repaid for Medicaid paid by the state on behalf of the beneficiary; and 4) the trustee of a Self-Funded SNT must have total discretion to pay, or refuse to pay, resources of the SNT to the beneficiary.

Pennsylvania’s Act 42 of 2005 (Act 42) now requires that before the funding of a Self-Funded SNT, all liens and claims in favor of the Department for repayment of Cash Assistance and MA must first be satisfied. No

provision in the Social Security Act requires that all such liens be satisfied prior to the creation of a SNT, although where the SNT is funded through the proceeds of a personal injury action Pennsylvania and federal law have long required that some or all of MA paid on account of the accident be repaid before any recovery is paid to the plaintiff or a Trust for the plaintiff. The Department has no formal "lien" to recover for MA payments which are unrelated to the accident. The DPW lien generally applies only to 1) recovery from an accident which must be available to repay MA for benefits provided as a result of the accident; and 2) MA provided after the age of 55, for which all probate assets must be available to repay the DPW. The "pay back" to DPW upon termination of a self-funded SNT is a separate issue involving different legal principals.

Any expenditure from a SNT must have a reasonable relationship to the needs of the beneficiary. This requirement appears to be designed to curb real or imagined "excesses" in the use of Self-Funded SNTs for extravagant luxuries.

As noted above, a Self-Funded SNT must state that monies in the SNT at the beneficiary's death will be made available to repay the state for MA payments made on behalf of the beneficiary during his/her lifetime. Upon the death of beneficiary or the termination of the Trust, the trustee must contact the Department, Third Party Liability Casualty Unit, SNT Depository at P.O. Box 8486, Harrisburg, PA 17105 or (717) 772-6257.

Where SSI eligibility is also an issue, and the beneficiary's own monies are used to fund the SNT, the SSI Guidelines consider the SNT to be revocable (and thus an available asset) unless a specific contingent beneficiary is named.

Pooled Trusts

Pooled SNTs must use a non-profit agency as trustee. The person with disabilities may establish a Self-Funded Trust without a parent, grandparent or guardian participating in the process. Under the federal statute no payback is required, but the residual resources are to remain in the Pooled SNT after the death of the beneficiary for the benefit of persons with disabilities.

Thorny Issues in the Creation and Maintenance of Special Needs Trusts

There are a number of thorny issues that arise during the creation and maintenance of SNTs. The following discussion outlines questions, issues and concerns ranging from preliminary matters to fixing broken SNTs.

Prior to creation, the appropriateness of a SNT must be determined. The following situations suggest the need to create a SNT, but can also suggest alternate approaches: 1) where the beneficiary is marginally disabled; 2) where the beneficiary does not currently receive SSI or MA, but may in the future; 3) where the trust corpus is relatively small, but the money can be spent down without losing eligibility; 4) where the trust corpus is so large that SSI and MA could be irrelevant and the SNT can be drafted in such a way as to pay out monies for food, shelter, and cash until the beneficiary requires MA/SSI; and 5) where other health benefits are currently available, for example, Medicare or Adult Basic.

A SNT should be seriously considered for a disabled beneficiary whenever that individual may receive 1) an inheritance; 2) an injury settlement; 3) a Social Security award for back benefits; 4) a compensatory education fund; and 5) a reversionary interest in property. It is also necessary to avoid combining assets of the person with disabilities with assets of or from third parties.

There a number of other complex questions that frequently arise during the creation of a SNT, including, but not limited to: 1) What must the Trustee know about administering the SNT? 2) Must the settlor have the legal authority to manage the assets of the disabled beneficiary? 3) What are the differing demands of the DPW, Social Security Administration and MH/ID? 4) What Social Security number do you use? 5) Who should be the contingent beneficiaries? and 6) How does an attorney petition the court to act as settlor for a Self-Funded SNT

when no parent, grandparent or guardian is available? The advice of experienced and competent counsel is essential in addressing these questions.

Where a SNT will be funded with very significant moneys, the settlor must decide whether to use a corporate or non-corporate trustee. If the settlor decides to utilize a corporate trustee, it must be determined which corporate trustee is best. In doing so, one should consider: 1) fees; 2) customer service history; 3) knowledge of SNTs and disability issues; and 4) investment strategies. It is important to recognize that financial demands upon the trustee by the beneficiary and the family can be difficult to address. These issues can include salaries for family members to care for the disabled beneficiary, housing for entire family, family vacations, vehicles not specially designed for the disabled beneficiary, food, rent/mortgage, cash for disabled beneficiary, and professional services.

The courts sometimes appoint a non-corporate trustee in matters involving a small recovery or inheritance for a minor or incapacitated person. In such cases the court may approve a family member, friend, financial planner or an attorney. In these circumstances, it should be determined whether any conflicts of interest are implicated before deciding upon a trustee. When naming a trustee of a smaller SNT, one should take into consideration how demanding the beneficiary or family circumstances may be and whether the trustee can handle the demands. Such a trustee will also need to address: 1) payment of fees to the trustee; 2) investment issues; and 3) supportive/intervention casework services to keep the trustee current on the beneficiary's circumstances and needs.

With respect to the beneficiary, a trustee of a SNT must question whether or not to accede to requests which will quickly deplete the corpus of the trust, whether the principal can properly be invaded, whether DPW would object to the beneficiary's requests, and how the corpus of the trust should be invested.

Other Thorny Issues

Fixing Improper SNTs or Annuities

The Department of Public Welfare and Social Security Administration are reasonable in reforming defective trusts so long as a new payback trust is created which gives the Department prior notice regarding expenditures of principal. A beneficiary or representative could also petition the court to reform the defective trust. The Structured Settlement Protection Act can also be used to transfer annuity payments to a Self-Funded Trust where the periodic payments disqualify a disabled beneficiary from public benefits. Notice must be given to all beneficiaries, and ideally such notice and consent should extend to residual beneficiaries.

Paybacks

As noted above, the Social Security Act requires repayment language for Medicaid expended during the term of a Self-Funded SNT. A SNT that is funded by parents or a third party source will generally not be required to pay back Medicaid. The only assets within a SNT that are subject to the repayment obligation are those assets which originally belonged to the disabled individual and are transferred into a Self-Funded SNT.

When creating a Self-Funded SNT, it is critical to plan for payback during trust administration and determine how to deal with the Department at the termination of the SNT.

Support Obligations of a Parent of a Child with a Disability

The existence of a SNT for a child with disabilities is generally not a factor in determining the support obligations of the parents of the child, and a parent cannot evade support obligations due to the existence of a SNT for the child. Moreover, distributions from a discretionary SNT to the disabled parent of a minor child may be considered "income" of that parent in calculating the parent's support obligation.

Structured Settlements

When using a structured settlement in an injury case, it is important to initially fund the SNT with sufficient “seed money” to address the following issues: 1) the settlor should have a broad choice of corporate trustees, but a minimal initial corpus will deter most such trustees; 2) sufficient resources must be immediately available to address unforeseen early needs of the beneficiary; and 3) the trustee must have enough available resources upon the death of beneficiary to pay death taxes and the payback to the Department. A structured settlement should arrange for a commutation clause to be effective upon the death of the beneficiary so that the estate can pay death taxes and administrative costs. One should also carefully identify the death beneficiary of a structured settlement which funds a Self-Funded SNT, because DPW now insists that the death beneficiary be the SNT, not a third party who could take the proceeds and evade the Department’s payback.

“Dual Eligibles” who receive MA

A client who receives Medicare but has limited income and resources may be “dually eligible” for MA, which can pay for Medicare’s Part B, Part D drug costs which are excluded from Medicare, and deductibles/copays.

Section 8 Housing

The Section 8 regulations focus mostly on income, which can include income from a trust fund for Section 8 housing. The value of irrevocable trust funds should not be considered an asset so long as the fund continues to be held in trust, and no member of the family or household can have control of the trust. However, any income distributed from the trust is counted when determining the family’s annual income.

Food Stamps

Resources having a cash value which is not accessible to the household, such as irrevocable trust funds, are generally excluded from the resources of a household.

General Assistance

If an individual receives General Assistance, usually while a recipient awaits a SSI determination, the DPW will generally disqualify for assets in Trust despite regulations which appear to exclude SNTs.

Rapid Spenddown of Funds Received From Injury Settlements, Inheritances, etc.

A rapid spenddown of funds received by a person with disabilities is used to maintain SSI and/or MA without use of a Self-Funded Trust. A rapid spenddown must occur during the calendar month of receipt of monies, and the individual must make expenditures and/or purchase assets for fair market value and keep receipts. This process can be complex and should occur with the advice of competent counsel.

Absence of a Parent, Grandparent or Guardian to Create a Self-Funded SNT

A court can create a Self-Funded SNT in the absence of a parent, grandparent or guardian, and in such cases, the court acts as the technical settlor. The court need not sign the SNT but should issue an order expressly approving and establishing the SNT. The trust must be drafted in a manner which is consistent with the court acting as the settlor.

Idiosyncrasies of the Social Security Administration

Some idiosyncrasies exist regarding Self-Funded Trusts and the Social Security Administration: 1) the SNT must have a named contingent beneficiary; and 2) an individual cannot use the SNT for funeral or burial of a deceased beneficiary except via prepaid funeral/burial plans.

In-Kind-Support-and-Maintenance-Payments for Food and Shelter

The Presumed Maximum Value Rule of the SSA generally limits reduction of SSI to about one-third of the maximum allowable SSI regardless of the amount of In-Kind-Support-and-Maintenance actually paid for food and shelter. The SNT should not reimburse the family for food and shelter; rather, the SNT should pay vendors directly or provide the family with a restricted credit card. This process can be very complex and should occur only with the advice of competent counsel.

Payments to Family Caregivers

Court approval should generally be obtained for payment to family members as caregivers. Reasonable rates must be used and should reflect replacement of lost income of the caregiver. In considering payments to family as caregivers, care must be taken in identifying the employer for purposes of tax withholding, worker's compensation, unemployment, etc.

Purchase of Homes

Approval of the court and DPW should generally be obtained when a Self-Funded Trust is used to purchase a home. The house should be titled in the name of the SNT. The use of the home, including taxes and essential utilities, will likely be considered In-Kind-Support-and-Maintenance, but its effect is often limited by the Presumed Maximum Value Rule. Questions that may arise when considering the purchase of a home include: 1) Will the trustee agree to manage the property? 2) What if the property's value declines due to neglect or due to a decline in the neighborhood's property values? and 3) Will a court require the family of a beneficiary who is a minor or incapacitated person to pay some rent/upkeep expenses?

Corporate Trustees

Since 1993 there has been an expansion of available, competent trustees who are either for-profit or non-profit fiduciaries. It should be noted that some trustees request a provision in the SNT which limits their liability for their negligence and which allows the trustee to use trust resources to pay for extensive outsourcing of typical trustee services such as investment advice or social work services, and some courts are unwilling to approve these provisions.

Marketing to Families with Children with Disabilities

Many investment companies now market insurance and a variety of investments to families of persons with disabilities.

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