

SPECIAL NEEDS TRUSTS AND THE SOLE BENEFIT RULE

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INTRODUCTION

The sole benefit rule is both the touchstone and the bane of special needs trust practitioners and trustees. This paper will provide a brief overview of special needs trusts for context before going on to define and examine the sole benefit rule with some reserved criticism. This initial examination will focus primarily on the rule as applied nationally through the Social Security Administration's Supplemental Security Income Program. Following an examination of resource rules, which form the basis of the sole benefit rule, this paper will then look at the rule in a sampling of states. The paper will conclude with some general observations on how the rule affects trust beneficiaries.

SPECIAL NEEDS TRUST OVERVIEW

Most special needs trust practitioners would agree that the confusion often attending special needs trusts is due to the complexity of public benefit rules and not due to the law of trusts. Even though the federal legislation authorizing the special needs trust exception was passed 21 years ago in 1993, the term is still not always clearly defined or used with great precision.¹ Because the sole benefit rule does not apply to all special needs trusts, it is worth taking a few minutes to make sure we have the necessary context before examining how the rule applies and how it affects the establishment and administration of special needs trusts.

The one special characteristic that all special needs trusts share is to create a fund that can supplement the beneficiary's care and quality of life while simultaneously protecting the trust beneficiary's eligibility for means tested public benefit programs such as Supplemental Security Income (SSI) and Medicaid.² They provide this protection through two overarching

¹ The Omnibus Budget Reconciliation Act of 1993 (OBRA '93) was passed by the 103rd Congress and signed into law by President Bill Clinton. The OBRA '93 provisions relating to special needs trusts are found in §1917(d)(4)(A)-(C) of the Social Security Act and are codified at 42 U.S.C. §1396p(d)(4)(A)-(C).

² The Medicaid program is found in Title XIX of the Social Security Act and at 42 U.S.C. §1396a through §1396w-5. Often confused with Medicare, Medicaid is a joint federal and state program that provides medical benefits to elderly and disabled individuals whose income and assets are below strict limits. Each of the states administers its own Medicaid program but receives matching federal dollars provided it continues to adhere to its state plan. The federal government's share varies from state to state but has historically averaged 57%. See *An Overview of the Medicaid Program* by the Congressional Budget Office at <http://www.cbo.gov/publication/44588>.

provisions. First, all special needs trusts are full discretionary trusts and therefore restrict the trust beneficiary from accessing trust funds or exercising control over their use. Second, all special needs trusts are established as either irrevocable trusts, or in the case of revocable trusts, with no power or revocation granted to the trust beneficiary. These are necessary provisions for all special needs trusts because, under the applicable resource counting rules, the availability of a resource is the beginning point for whether or not that asset counts against SSI and Medicaid eligibility.³

Moving beyond the common trait of protecting public benefit eligibility, the characteristic that begins to distinguish special needs trusts is based on the source of their funding. Special needs trusts that are funded with assets originally belonging to the trust beneficiary are commonly referred to as self-settled or first party special needs trusts, and they must always be established to conform with the statutory requirements found in 42 U.S.C. §1396p(d)(4)(A) or (C).⁴ Among practitioners, these trusts are very often specifically referred to as (d)(4)(A) or (d)(4)(C) trusts to indicate the controlling section of the statute.

Pursuant to (d)(4)(A), the normal rules that count trusts as an available resource will not apply to a trust that:

- a) contains the assets of an individual under age 65 who is disabled as defined in U.S.C. 42 §1382c(a)(3);
- b) is established for the benefit of the individual;
- c) is established by the individual's parent, grandparent, legal guardian, or a court; and,

(last accessed October of 2014). Like Medicaid, SSI also imposes strict income and asset limits but it is administered solely by the federal government through the Social Security Administration. SSI pays a monthly check instead of providing medical benefits, and the maximum amount of any check is the full federal benefit rate of \$721.00 in 2014. SSI has a complex method for counting income, but for each dollar of countable income, an individual's check will be reduced by one dollar.

³ 20 C.F.R. § 416.1201(a) defines resources as, "...cash or other liquid assets or any real or personal property that an individual (or spouse, if any) owns and could convert to cash to be used for his or her support and maintenance. If the individual has the right, authority or power to liquidate the property or his or her share of the property, it is considered a resource. If a property right cannot be liquidated, the property will not be considered a resource of the individual (or spouse)." See also, *Hunt v. Astrue*, D.Mass.2008, 581 F.Supp.2d 238. A trust that named a SSI applicant as the sole beneficiary was determined to be a countable resource and therefore precluded SSI eligibility because, under Massachusetts law, the trust was revocable by the beneficiary or his legal guardian and the beneficiary could direct that the trust be used for his support or maintenance.

⁴ The statutory requirements for establishing special needs trusts under §1396p(d)(4)(A) and pooled trusts under §1396p(d)(4)(C) are facially straightforward, but these requirements are not uniformly interpreted or applied by Medicaid Administrators across the country. §1396p(d) creates an additional exception trust at sub-paragraph (B), but this trust is not relevant to a discussion of the sole benefit rule because it only holds income under limited circumstances. In states that impose income limits on Medicaid benefits for long term nursing home care or Home and Community Based Services, the monthly income limit is \$2,163 in 2014. In such states, an individual who is ineligible for these benefits due to excess income can become eligible by establishing a (d)(4)(B) trust and funding it each month with their excess income. These trusts are commonly called Miller trusts or Qualified Income Trusts.

- d) is required by its terms to use any remaining assets upon the individual's death to reimburse the state for all of the medical assistance paid on behalf of the individual under a state plan.

Similarly, pursuant to (d)(4)(C), the normal rules that count trusts as an available resource will not apply to a trust that:

- a) is established and managed by a nonprofit association;
- b) maintains a separate account for each beneficiary but pools the funds for investment and management purposes;
- c) establishes accounts solely for the benefit of individuals of any age who are disabled as defined in U.S.C. 42 §1382c(a)(3);
- d) has individual accounts established by the parent, grandparent, or legal guardian of the individual, by the individual, or by a court; and,
- e) specifically provides to the extent that any remaining assets are not retained by the trust upon the individual's death, they must be used to reimburse the state for all of the medical assistance paid on behalf of the individual under a state plan.

In contrast to self-settled (d)(4)(A) and (d)(4)(C) special needs trusts, trusts that are funded with assets originally belonging to someone other than the trust beneficiary are commonly referred to as third party special needs trusts.⁵ Third party special needs trusts can be created as inter-vivos or testamentary trusts. They can also be established as a stand alone revocable or irrevocable trust for a single beneficiary or as a share created within a trust with multiple beneficiaries. In the case of a trust with two or more beneficiaries, only the share granted to the beneficiary receiving SSI or Medicaid needs to be designated as a special needs trust and administered accordingly. Such a trust would be a discretionary trust as to the share of the special needs beneficiary, but the grantor would otherwise be free to designate the management and disposition of the remaining trust as meets his or her more general estate planning objectives.

The distinction between self-settled and third party special needs trusts can be a significant one for a number of estate planning reasons. However, as it relates to the sole benefit rule, the important distinction is to recognize that third party special needs trusts are not subject to the rule. As will be explained in more detail below, only (d)(4)(A) and (d)(4)(C) trusts are subject to the sole benefit rule because they are self-funded.

⁵ Unlike (d)(4)(A) and (d)(4)(C) trusts, the United States Code does not provide a list of specific criteria that third party special needs trusts must meet. The relevant portion of the statute on the treatment of trusts simply provides that, "...an individual shall be considered to have established a trust if assets of the individual were used to form all or part of the corpus of the trust..." when the trust is established by the individual, a spouse, anyone with the authority to act on behalf of the individual or spouse, or anyone acting on the direction or request of the individual or spouse. 42 U.S.C. §1396p(d)(2)(A). See however, POMS SI 01120.200B.17, which provides a more straightforward definition, "[A] third-party trust is a trust established with the assets of someone other than the beneficiary." The only exception to this general rule is that a testamentary trust will never be treated as having been established by the individual, even if established by the Will of a spouse. 42 U.S.C. §1396p(d)(2)(A).

THE SOLE BENEFIT RULE WITH ACCOMPANYING COMMENT

For purposes of Medicaid, the sole benefit rule is implemented with some variation from state to state because each state is responsible for administering its own Medicaid program. While we will look at some state specific examples in a later section, for now we will begin by looking at how the rule is defined and implemented by the Social Security Administration (SSA) in the administration of its SSI program. Because the SSA is an agency of the federal government, its SSI rules are in theory uniform across the country. Therefore, beginning with SSI will give us the best approximation of a national standard.

A plain reading of 42 U.S.C. §1396p(d)(4)(A) and (C) seems to recite a set of relatively simple and straightforward requirements. In terms of the beneficial interests that must be created, sub-paragraph (A) only requires that a special needs trust be, "...established for the benefit of such individual...." Likewise, for a pooled special needs trust, sub-paragraph (C) only requires that, "...accounts in the trust are established solely for the benefit of individuals who are disabled...." However, the policy manual used by employees at the SSA adds an additional layer to these seemingly straightforward requirements. The SSA policy manual is called the Policy Operations Manual System (POMS), and it is the official SSA reference used to process Social Security claims and to interpret federal law and regulations regarding SSI and all other Social Security Benefits.

While the POMS do not have the force of law, courts have long relied on agency interpretations regarding SSI and Medicaid.⁶ While there have been interesting arguments advanced that the SSA is not entitled to deference regarding its interpretation of trusts, for the present and foreseeable future, special needs trusts and pooled trusts must comply with the POMS in addition to the plain language of the federal statute.⁷ From a purely practical perspective, complying with the POMS is necessary so that a trust will pass review when submitted to the SSA. It is important for drafting attorneys to be diligent in this regard because SSA employees will not be swayed by arguments that any particular section of the POMS fails to comport with federal law or regulations. Passing review by the SSA is critical for the trust beneficiary because the entire trust corpus will be characterized as an available resource in any case where the SSA determines that a trust fails to meet all of the necessary requirements.

⁶ The Social Security Administration's interpretation of disability was upheld in a case involving the agency's denial of claim for disability benefits. The Supreme Court held that where an Act is " 'silent or ambiguous' with respect to a specific issue, [the courts] must defer to a reasonable construction by the agency charged with its implementation". *Barnhart v. Thomas*, 540 U.S. 20, 26, 124 S.Ct. 376, 157 L.Ed.2d 333 (2003) (citing *Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc.*, 467 U.S. 837, 843, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984)). See also, *Schweiker v. Gray Panthers*, 453 U. S. 34, 43. In reversing the Court of Appeals for the District of Columbia Circuit, Justice Powell stated, "Congress explicitly delegated to the Secretary broad authority to promulgate regulations defining eligibility requirements for Medicaid. We find that the regulations at issue in this case are consistent with the statutory scheme and also are reasonable exercises of the delegated power."

⁷ Landsman, Ron. "When Worlds Collide: State Trust Law and Federal Welfare Programs." *NAELA Journal* Volume 10.1 (2014): 25-50. Print.

The additional layer added to the plain language of the federal statute is found in two different but related sections of the POMS. Beginning with the first section, which is found in sub-paragraph B.1.e. of SI 01120.203 *Exceptions to Counting Trusts Established on or after 1/1/00*, the POMS tell us that:

Under the special needs trust exception, the trust must be established for and used for the benefit of the disabled individual. SSA has interpreted this provision to require that the trust be for the **sole benefit** of the individual, as described in SI 01120.201F.2 (emphasis added).

This same sub-paragraph goes on to instruct SSA employees that if the trust includes any provisions that:

- provide benefits to other individuals or entities during the disabled individual's lifetime, or
- allow for termination of the trust prior to the individual's death and payment of the corpus to another individual or entity (other than the State(s) or another creditor for payment for goods or services provided to the individual), will result in disqualification for the special needs trust exception.

The last part of sub-paragraph B.1.e. authorizes vendor payments made to third parties if the trust beneficiary will receive the goods or services that are purchased, but it also includes a caution. More specifically, it cautions SSA employees to evaluate any such payments under the normal SSI income rules for a determination of whether or not the payments constitute countable income to the trust beneficiary.

The second POMS section is found in SI 01120.201, *Trusts established with the assets of an individual on or after 1/1/00*. This is the section to which SI 01120.203 above cites, and it defines what it means for a trust to be established for the sole benefit of an individual.

Consider a trust 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 (emphasis in the original).

Except as provided in SI 01120.201F.2.b. in this section and SI 01120.201F.2.c. in this section, do not consider a trust that provides for the trust corpus or income to be paid to or for a beneficiary other than the SSI applicant/recipient to be established for the sole benefit of the individual.

So to paraphrase or state the rule, a special needs trust is required by its terms to benefit no one but the trust beneficiary at the time the trust is established or at anytime during the beneficiary's lifetime. While this does not necessarily sound inconsistent with a trustee's duty of loyalty to a beneficiary, the SSA introduces unnecessary complications by expressing a view that runs counter to more traditional concepts of what it means for someone to benefit from a trust. This view is expressed by what SI 01120.201 goes on to describe in sub-paragraphs F.2.b. and F.2.c. as exceptions to the sole benefit rule. Sub-paragraph F.2.b. is set out below in its entirety with F.2.c. following shortly thereafter.

b. Exceptions to the sole benefit rule for third party payments

Consider the following disbursements or distributions to be for the sole benefit of the trust beneficiary:

- Payments to a third party that result in the receipt of goods or services by the trust beneficiary;
- Payment of third party travel expenses which are necessary in order for the trust beneficiary to obtain medical treatment; and
- Payment of third party travel expenses to visit a trust beneficiary who resides in an institution, nursing home, or other long-term care facility (e.g., group homes and assisted living facilities) or other supported living arrangement in which a non-family member or entity is being paid to provide or oversee the individual's living arrangement. The travel must be for the purpose of ensuring the safety and/or medical well-being of the individual.

NOTE: If you have questions about whether a disbursement is permissible, please request assistance from your regional office.

The first bullet point on third party payments is consistent with traditional concepts of what it means for a trust to provide a benefit for a beneficiary. The troubling issue, however, is that the SSA describes these payments as an exception to the sole benefit rule. SSA employees are instructed to “consider” such payments as being for the trust beneficiary’s sole benefit as if the beneficiary is not in fact receiving a real trust benefit from such payments. While it might seem reasonable to give the SSA the benefit of the doubt and attribute this POMS provision to inexact drafting, the remaining provisions suggest a misunderstanding of trusts and a bias against their use by SSI recipients. This same misunderstanding and bias is also frequently evident when interacting with the SSA.

The second and third bullet points both address the issue of paying third party travel expenses in slightly different contexts. The second point disallows travel expenses for third parties who might otherwise accompany a trust beneficiary, while the third point disallows travel expenses for third parties who might otherwise visit a trust beneficiary. What is consistent about both provisions is the requirement that third party travel expenses always be necessary for ensuring the trust beneficiary’s medical care or safety in some fashion. Moreover, the third bullet point imposes an additional condition that the trust beneficiary reside in a nursing home or other supported living arrangement.

While no competent and conscientious special needs trust trustee would thoughtlessly approve the use of trust funds for a trust beneficiary’s entire family, imposing the condition of medical necessity simply fails to recognize other travel situations in which the trust beneficiary would receive a tangible and primary benefit from the trust. Consider the following example. A nine year old girl with severe disabilities has recently settled her medical malpractice action for birth-related injuries, and her settlement proceeds were used to fund a court approved special needs trust. She lives in a single parent household with her mother, and her dream for the past several years has been to visit Disney World. There is no question about the trip being

affordable for her trust, but it will be impossible for her to make such a trip without her mother or another companion. Absent the societal tendency to believe that poor and disadvantaged people merit punishment, it is hard to imagine that a trust disbursement that includes travel expenses for her mother would fail to be for the primary benefit of the little girl.

Also consider the example of an eighty-four year old beneficiary who cannot travel and wants his trust to pay travel expenses so his eighty-two year old brother can visit. The eighty-two year old brother does not have the ability to pay his own expenses, the two brothers have not seen each other since their mother's funeral 20 years ago, and they are the last surviving siblings in their family. Even though the eighty-two year old brother will receive a secondary benefit, it is the only way to provide a primary benefit for the trust beneficiary. It is difficult to doubt the emotional and psychological benefit such a payment would provide to the trust beneficiary when his trust is the only option for him to see his brother for what will very likely be the last time.

Returning to section SI 01120.201 of the POMS, sub-paragraph F.2.c. provides the last exception to the sole benefit rule.

c. Exceptions to the sole benefit rule for administrative expenses

The trust may also provide for reasonable compensation for a trustee(s) to manage the trust, as well as reasonable costs associated with investment, legal or other services rendered on behalf of the individual with regard to the trust. In defining what is reasonable compensation, consider the time and effort involved in providing the services involved, as well as the prevailing rate of compensation for similar services considering the size and complexity of the trust.

As with the exception for third party payments, this section of the POMS creates an exception for certain administrative expenses. Again, to create an exception for such expenses is to imply that an exception is necessary because the beneficiary does not receive a trust benefit for the payment of these services. The perceived need for this exception seems to express a mistaken view that paying administrative expenses is to confer a trust benefit on the trustee as opposed to merely paying for a service provided to the trust beneficiary.

The POMS also describes how the sole benefit rule applies to (d)(4)(C) pooled trusts in addition to (d)(4)(A) special needs trusts. Pooled trusts are described in SI 01120.203B.2., and sub-paragraph e. echoes the requirements for special needs trusts as follows.

Under the pooled trust exception, the individual trust account must be established for the sole benefit of the disabled individual. (For a definition of sole benefit, see SI 01120.201F.2). Other than the payments described in SI 01120.201F.2.b. and SI 01120.201F.2.c., this exception does not apply if the trust account:

- provides a benefit to any other individual or entity during the disabled individual's lifetime, or
- allows for termination of the trust account prior to the individual's death and payment of the corpus to another individual or entity.

The POMS citations in the section above direct the reader back to the same sections previously examined in regard to special needs trusts. Namely, the definition of the sole benefit rule and the third party payments that are exceptions to the sole benefit rule. The section above, however, puts a slightly finer point on the issue by prohibiting any benefit, "...to any other individual or entity...", and by adding a specific prohibition on early termination provisions. Early termination provisions are sometimes used by practioners to provide for the contingency of a trust beneficiary no longer needing or wanting SSI or Medicaid in the future.

Effective May 14, 2013, the SSA provided further clarification on its early termination prohibition with POMS SI 01120.199, *Early Termination Provisions and Trusts*. According to this POMS section, trusts that otherwise meet the special needs or pooled trust exceptions will need to meet another set of criteria if they contain early termination provisions. Rather than provide a full citation, this set of criteria is paraphrased below. If a trust is terminated prior to the death of the beneficiary:

1. the state(s) must receive any remaining amounts up to the full amount of medical assistance paid on behalf of the trust beneficiary;
2. all of the remaining funds must be paid to the trust beneficiary, and no other person or entity is permitted to benefit from the early termination; and,
3. the early termination clause can only be exercised by someone other than the trust beneficiary.⁸

RESOURCE RULES

A. Resource Limits

With the exception of certain limited exclusions, SSI and Medicaid both impose strict resource limits as a condition to eligibility.⁹ Each program also imposes income rules, but these rules are beyond the scope of this paper and are not relevant to a discussion about the sole benefit rule. By contrast, the resource rules are relevant to a discussion about the sole benefit rule because the resource rules place restrictions on transferring resources for less than fair market value. Following a brief overview of the resource limits, we will examine how these transfer restrictions relate to and inform the sole benefit rule.

The resource rules for SSI are found in 42 U.S.C. §1382 and begin in paragraph (a) where an eligible individual is defined as:

⁸ For any trust that the SSA previously determined was exempt from the resource counting rules prior to SI 01120.199 being implemented, a 90 day grace period is provided for the trust to be amended. The grace period begins from the day the SSA notifies the trust beneficiary or their representative that the trust needs to be amended.

⁹ For example, both programs exclude an individual's home, household goods, personal effects, one automobile, burial spaces, irrevocable pre-need burial agreements, and other property that is essential to self-support. For the Medicaid program, however, specific details may vary from state to state. See, 42 U.S.C. §1382b (SSI).

(1) Each aged, blind, or disabled individual who does not have an eligible spouse and--

(A) - omitted because it applies to income

(B) whose resources, other than resources excluded pursuant to section 1382b(a) of this title, are not more than (I) in case such individual has a spouse with whom he is living, the applicable amount determined under paragraph (3)(A), or (ii) in case such individual has no spouse with whom he is living, the applicable amount determined under paragraph (3)(B),

Turning to paragraph (3)(B), the resource limit of \$2,000 is confirmed after allowing for any of the applicable exclusions allowed by 1382b.

(B) The dollar amount referred to in clause (ii) of paragraph (1)(B), shall be \$1,500 prior to January 1, 1985, and shall be increased to \$1,600 on January 1, 1985, to \$1,700 on January 1, 1986, to \$1,800 on January 1, 1987, to \$1,900 on January 1, 1988, and to \$2,000 on January 1, 1989.

In terms of what counts as a resource, it bears repeating the definition that is provided by the cite to 20 C.F.R. § 416.1201(a) above footnote 3. Resources include:

...cash or other liquid assets or any real or personal property that an individual (or spouse, if any) owns and could convert to cash to be used for his or her support and maintenance. If the individual has the right, authority or power to liquidate the property or his or her share of the property, it is considered a resource.

Regarding Medicaid, the resource rules do not lend themselves to the same easy isolation as the SSI rules because each state is left to determine its own eligibility standards within certain federal constraints. As a condition to receiving matching federal funds, each state must submit a state plan to the Center for Medicare and Medicaid Services (CMS). As a condition to approval, a state plan must describe how the state will meet all the requirements of federal law. Among other things, these requirements include the identification of eligibility groups that will be covered, the types of services that will be provided, how providers will be reimbursed, and technical and financial eligibility requirements.¹⁰

Requiring states to submit state plans introduces some state by state variation, but as with SSI, state Medicaid programs have very restrictive financial eligibility requirements. The Social Security Act gives states the option of using either the SSI criteria to determine Medicaid eligibility or using at least one criterion that is more restrictive than SSI. States that use the SSI criteria are referred to as SSI states, and states that opt for at least one more restrictive criteria

¹⁰ See the Social Security Act §1902(a) and 42 U.S.C. §1396a for the requirement of state plans generally and also for the identification of general financial eligibility standards for various coverage groups. See also 42 C.F.R. §435.2 for the general eligibility provisions that state plans must contain and 42 C.F.R. §§435.601-435.601 for more specific financial eligibility requirements.

are referred to as 209(b) states.¹¹ Among the SSI states, Section 1634 of the Social Security Act authorizes states to enter agreements with the SSA that gives the SSA right to make eligibility determinations for Medicaid at the same time it determines eligibility for SSI. These agreements are called 1634 agreements, and the states that enter them are called 1634 states. Of the 40 states who use SSI criteria, 33 are 1634 states.

B. Transfer Rules

Unlike the manner in which the resource limits are circumscribed for Medicaid, the rules that prohibit uncompensated transfers for both SSI and Medicaid are plainly stated.

1. SSI

An individual is ineligible for SSI benefits if he or she, “...disposes of resources for less than fair market value on or after the look-back date....”¹² The look-back date is 36 months before the individual applies for benefits, or later, if the individual or spouse disposes of assets subsequent to the application being filed.¹³ The penalty period during which an individual is ineligible for benefits begins in the month of the transfer, and its length is calculated by dividing the full benefit rate, plus any state supplementary payments, into the total value of the resources disposed of for less than fair market value.¹⁴ For example, an individual who transfers a \$60,000 personal injury settlement or inheritance to a friend or family member would incur a penalty period of 83 months ($60,000 / 721 = 83.22$ rounded down to 83). Fortunately for the individual in this example, the penalty period for SSI is capped at 36 months.¹⁵

2. Medicaid

State plans are required to provide that an institutionalized individual will be ineligible for medical services if the individual, or the individual’s spouse, disposes of assets for less than fair market value on or after the look-back date. At the option of the state, the state plan can also make noninstitutionalized individuals who dispose of assets ineligible for medical services.¹⁶ The look-back date is 36 months for transfers occurring before February 8, 2006 and 60 months for

¹¹ Title XIX of the Social Security Act, which created the Medicaid program, was signed into law on July 30, 1965, by President Johnson. By contrast, the SSI program was not added to the Act until 1972. The Social Security Amendments creating the SSI program also set national standards for three of the four categorical coverage groups entitled to Medicaid. To avoid an automatic increase in state Medicaid eligibility levels, § 209 of the Social Security Amendments gave states the option of retaining their original Medicaid eligibility standards. Social Security Amendments of 1972, Pub. L. No. 92-603, § 209(b). There are currently ten 209(b) states: Connecticut; New Hampshire; Hawaii; Illinois; Minnesota; Missouri; North Dakota; Ohio; Oklahoma; and Virginia.

¹² 42 U.S.C. §1382b(c)(1)(A)(I).

¹³ *Id.* at (1)(A)(I) and (II).

¹⁴ *Id.* at (1)(A)(II)(iii), (iv)(I), and (II).

¹⁵ *Id.*

¹⁶ 42 U.S.C. §1396p(c)(1)(A).

transfers occurring after this date.¹⁷ Just as the look-back date differs depending on the date of the transfer, so too, the beginning of the penalty period also differs depending on the date of the transfer. For transfers occurring before February 8, 2006, the penalty period begins on the first day of the month the transfer was made. For transfers occurring after this date, the penalty period begins on the later of either the first day of the month the transfer was made or the date on which the individual would otherwise be eligible to receive benefits but for the application of the penalty period.¹⁸

Like the SSI transfer penalty, the Medicaid penalty is calculated by applying a divisor to the total, “...value of all assets transferred by the individual (or spouse) on or after the look-back date...”¹⁹ However, a different divisor is applied to the total value of the transferred resources. Instead of using the full federal benefit rate, the average monthly cost of private nursing home care is used as a divisor. This divisor is currently \$7,995.00 in Florida, but it can vary widely from state to state. Not only does the actual cost of care vary, although it is very expensive everywhere, but state Medicaid agencies do not always update the divisor as they are required. Applying this divisor to our SSI example above will obviously produce a very different result. Instead of an 83 month penalty period, or period capped at 36 months, transferring \$60,000 will only result in a penalty period of 7.5 months ($60,000 / 7,995 = 7.5$). This shorter penalty period would be an especially favorable difference for a Medicaid applicant because, unlike SSI, the penalty period for Medicaid is not capped and is not rounded down.

C. Exceptions to the Transfer Rules

Although the transfer rules work to impose different penalty periods for SSI and Medicaid, the exceptions to these transfer rules are virtually the same for each program. For example, both programs specifically list circumstances that will not result in a period of ineligibility if an individual transfers his or her home for less than fair market value. Both programs also specifically list circumstances when transferring resources other than the home is permissible. In both cases, the statutory language is nearly identical, which allows them to be accurately described and discussed together.²⁰

An individual is permitted to transfer his or her home penalty free if the transfer is made to:

1. the individual’s spouse;
2. child who is blind or disabled and under 21 years of age;

¹⁷ *Id.* at (c)(B)(I).

¹⁸ *Id.* at (D)(i) and (ii). The amendments that created this longer look-back period and the change in the beginning of the penalty period were included within the Deficit Reduction Act of 2005 and were part of a larger effort to toughen up the Medicaid eligibility rules.

¹⁹ *Id.* at (c)(1)(E)(i)(I) and (II).

²⁰ See § 1382b(c)(1)(C)(i) and (ii) for the SSI exceptions and § 1396p(c)(2)(A) and (B) for the Medicaid exceptions.

3. sibling who has an equity interest in the home and resided in the home for at least one year prior to the individual becoming institutionalized; or,
4. a child of any age who lived in the home for at least two years prior to the individual becoming institutionalized and who provided care that allowed the individual to remain at home.

Regarding all other resources other than the home, penalty free transfers may be made as follows below:

1. to the individual's spouse or to another person for the sole benefit of the individual's spouse;
2. from the individual's spouse to another person for the sole benefit of the individual's spouse,
3. to a trust, including a trust described in §1396p(d)(4), that is established solely for the benefit of the individual's child who is blind or disabled; or,
4. to a trust, including a trust described in section §1396p(d)(4), that is established solely for the benefit of an individual who is disabled and who is under 65 years of age.

As noted above, the statutory language regarding permissible transfers is nearly identical for both SSI and Medicaid.²¹ Likewise, the statutory language is also similar in both regards in the sense that “sole benefit” is not defined. A careful reading of the transfer rules in both statutes only reveals two instances of the use “for the sole benefit,” and two instances of the use, “solely for the benefit.” Although the statute does not clearly define the term, a definition was provided shortly after OBRA '93 was passed by Congress in 1993 when the Health Care Financing Administration issued State Medicaid Manual, “Transmittal 64” (Transmittal 64).²²

According to Transmittal 64, §3257, *Transfers of Assets and Treatment of Trusts*, subparagraph B.6. provides that:

[A] transfer is considered to be for the sole benefit of a spouse, blind or disabled child, or a disabled individual if the transfer is arranged in such a way that no individual or entity except the spouse, blind or disabled child, or disabled individual can benefit from the

²¹ *Id.*

²² On June 14, 2001, the Health Care Financing Administration (HCFA) issued a press release that its name was changed to the Centers for Medicare & Medicaid Services (CMS).

assets transferred in any way, whether at the time of the transfer or at any time in the future.²³

Elder law attorneys have continued to debate and contest various provisions of Transmittal 64, including the provision above, but for purposes of this paper, we have arrived at a generally accepted definition of sole benefit after examining the resource and transfer rules for SSI and Medicaid. So, to restate the rule for purposes of its application by the SSA for the SSI program, a special needs trust is required by its terms to benefit no one but the trust beneficiary at the time the trust is established or at anytime during the beneficiary's lifetime. We will now turn our attention to a sampling of states to compare some of the variation in how the rule is applied to Medicaid.

STATE SAMPLING

While most of the states consistently use the same definition for the sole benefit rule, they frequently add their own interpretation on how its application affects trusts. We will examine the trust rules and sole benefit definition used in Alabama, Connecticut, Maine, Maryland, New Jersey, Ohio, South Carolina, and Texas. What should emerge is a pattern that consistently reflects the federal rules but that also shows some states staying close to the plain language of 42 U.S.C. §1396p(d)(4)(A) and (C) while others vary widely in what they add to this plain language.

A. Alabama - a 1634 State

The state agency responsible for administering Medicaid in Alabama called the Alabama Medicaid Agency (the Agency). The general provisions implementing the Medicaid program in Alabama are found at Code of Ala. 1975, §§22-6-1, et seq., and the program rules are found in the Alabama Administrative Code.

1. Trust Rules

Rule No. 560-X-25-.08. *Development of Ownership Interest in Liquid Resources for SSI-Related Individuals.*

(1) - (3) omitted

(4) Trusts - Whether the principal of a trust is a resource to the applicant/recipient depends on its availability to the applicant/recipient by the terms of the trust instrument itself.

²³ Transmittal 64 is not as readily accessible on the internet as are most statutes and regulations, but it can be accessed at <http://www.sharinglaw.net/elder/Transmittal64.htm> (last accessed in October of 2014).

Trusts or other similar legal devices may be excluded from consideration as a resource. Medicaid shall determine whether the requirements for exclusion expressed in the current statutory authorities have been met.

560-X-25-.09 Transfer Of Assets Affecting Eligibility.

(1) - (7) omitted

(8) Transfers Not Considered. An individual shall not be ineligible for medical assistance to the extent that:

(a) - (d) omitted

(e) The assets were transferred to a trust which is determined to be exempt from consideration under §1917(d) of the Social Security Act.

What is missing from the Admin. Code provisions above is any specific detail on how the Agency actually determines, "...whether the requirements for exclusion expressed in the current statutory authorities have been met." The author contacted the Agency by email after failing to find any such information on the Agency's website and was told the information is not made available to the public because it is considered internal Agency information.²⁴

2. Sole Benefit Definition

Rule No. 560-X-25-.09 Transfer Of Assets Affecting Eligibility.

(11)(h) "For the sole benefit of: "A transfer is considered to be for the sole benefit of a spouse, or a blind or disabled child, if the transfer is arranged in such a way that no individual or entity, except the spouse or the blind or disabled child, can benefit from the assets transferred in any way, whether at the time of the transfer or any time in the future.

B. Connecticut - a 209(b) State

The state agency responsible for administering Medicaid in Connecticut is the Department of Social Services (the Department). Sec. 17b-10 of the Connecticut General Statutes requires the Department to "...prepare and routinely update state medical services and public assistance manuals." The manuals are not published in Connecticut's Administrative Code, but as part of its mandate to maintain policy manuals, the Department uses Connecticut's

²⁴ Email response from the Alabama Medicaid Agency on October 2, 2014, which was also copied to two other Agency personnel. The author's followup reply and second request with a detailed explanation that the requested material was for inclusion in this paper went unanswered. Absent any specific information, it is not possible to determine strictly from the broad language of the Ala. Admin. Code how the Agency interprets or implements policy.

Administrative Code to explain how its Policy Manual was adopted. The Code also contains a Table of Contents from the Policy Manual to help people find additional information.²⁵

The chapters of the Connecticut Department of Social Services Uniform Policy Manual on trusts and the definition of sole benefit, which are produced below, closely track the federal code and the POMS.

1. Trust Rules

4030.80 D

6. The Department does not consider the following types of trusts in determining the individual's eligibility for Medicaid:

a. a trust containing the assets of an individual under age 65 who is disabled, according to criteria under the SSI program, if:

(1) the trust is established for the benefit of such individual by his or her parent, grandparent, or legal guardian, or by a court acting in accordance with the authority of state law; and

(2) under the terms of the trust, the state will receive all amounts remaining in the trust upon the death of the individual, up to an amount equal to the total amount of Medicaid benefits paid on behalf of the individual.

b. a trust that meets the following conditions:

(1) the trust is established and managed by a non-profit association; and

(2) a separate account is maintained for each beneficiary of the trust, but, for purposes of investment and management of the funds, the trust pools these accounts; and

(3) accounts in the trust are established solely for the benefit of individuals who are disabled, according to criteria under the SSI program, by the individuals, their parent, grandparent or legal guardian, or by a court; and

(4) to the extent that the amounts remaining in the individual's account upon his or her death are not retained by the trust, the trust is required by

²⁵ Connecticut Administrative Code, Title 17, Sec. 17b-10-1. Uniform policy manual.

its terms to pay to the state from such remaining amount, an amount equal to the total amount of Medicaid benefits paid on behalf of the individual.

2. Sole Benefit Definition

3029.10 J.

"For the Sole Benefit of"

The phrase "for the sole benefit of" and individual, as described in 3029.10 B, C and D, means that the asset, trust or similar device benefits no one but the individual, either at the time the transfer or establishment of the trust, or at any time in the future, except as described below.

1. With respect to the establishment of a trust, the trust may provide for a reasonable fee to be paid to the trustee for managing the trust.
2. If a beneficiary is named to receive the transferred asset, or whatever is left of it, at the time of the individual's death, the transfer or trust is still considered to have been made for the sole benefit of the individual if:
 - a. the Department is named as the primary beneficiary of the asset, up to the amount of Medicaid payments paid on behalf of the individual; and
 - b. the designated beneficiary or beneficiaries receive any amount that remains.

C. Maine - a 1634 State

The state agency responsible for administering Medicaid in Maine, which the state calls MaineCare, is the Department of Health and Human Services (DHHS). The MaineCare Eligibility Manual is contained in chapter 332 of the Code of Maine Rules. The rules on special needs trusts and pooled trusts, which follow below, are found in 10-144 Chapter 332: MaineCare Eligibility Manual, Part 16 - Assets, which closely tracks the federal code.

1. Trust Rules

F. Exemptions

The following trusts are exempt from the provisions of (E) above. No transfer is considered to take place as a result of establishing the trust, except as indicated in 2. (below) relating to pooled trusts. The income and resources considered available to the individual are those made available by the trust.

1. a trust containing the assets of an individual under age 65 who does or would meet the SSI criteria for disability if:

- a. the trust is established for the sole benefit of the individual by the individual's parent, grandparent, legal guardian or a court; and
- b. the state will receive all amounts remaining in the trust upon the death of the individual up to an amount equal to the total Medicaid paid on behalf of the individual after due payment of any legal obligations of trust.

This trust is considered to be established for the "sole benefit of" the individual if no other individual or entity can benefit from the assets transferred in any way whether at the time the trust is established or at any time in the future. A trust may provide for reasonable compensation to trustees to manage the trust and for beneficiaries after Medicaid has been reimbursed.

The trust may contain assets of individuals other than the disabled individual.

This exemption remains once the individual turns age 65 as long as there are no changes in the terms of the trust once the individual attains age 65. Any assets added as of age 65 are not subject to exemptions under (E) above.

2. a trust containing the assets of an individual who does or would meet the SSI criteria for disability if:
 - a. the trust is established and managed by a non-profit association;
 - b. a separate account is maintained for each beneficiary of the trust but for purposes of investment and management of funds, the trust pools these accounts;
 - c. the accounts in the trust are established solely for the benefit of the disabled individual by the individual or the individual's parent, grandparent, legal guardian or by a court; and
 - d. to the extent that amounts remaining in the beneficiary's account upon the death of the beneficiary are not retained by the trust, the trust pays to the state an amount equal to the total amount of Medicaid paid on behalf of the beneficiary after due payment of any legal obligations of the trust.

However, any assets added to the trust as of age 65 may be subject to a transfer penalty (see Part 15).

A trust is considered to be established for the "sole benefit of" the individual if no other individual or entity can benefit from the assets transferred in any way whether at the time the trust is established or at any time in the future. A trust may provide for reasonable compensation to trustees to manage the trust and for beneficiaries after Medicaid has been reimbursed.

An individual age 65 or older is not automatically considered to meet the SSI criteria for disability. This must be determined as in Part 6, Section 4.3.

2. Sole Benefit Definition

Just as the MaineCare Eligibility Manual closely tracks the federal rules on trusts, it also closely follows the transfer rules and provides a definition of sole benefit in 10-144 Chapter 332:, Part 15 - Transfer of Assets. Section 1.4 provides that:

A transfer is considered to be for the "sole benefit of" a spouse, blind or disabled child or disabled individual when no individual or entity except the spouse, blind or disabled child or disabled individual can benefit from the assets transferred in any way, whether at the time of the transfer or at any other time in the future.

D. Maryland - a 1634 State

The state agency responsible for administering Medicaid in Maryland is the Department of Human Resources (DHR). The State of Maryland Medical Assistance Manual at 800.16 and Title 10 of the Code of Maryland Regulations (COMAR) at 10.09.24.08 contain the trust rules and transfer rules. The Manual provisions are provided below, which are mirrored very closely in COMAR. As seen by the material below, which continues to nearly to the bottom of page 24, Maryland has added very extensive conditions to the plain language of 42 U.S.C. §1396p(d).

1. Trust Rules

800.16

(a) Trust for Disabled Persons Under Age 65

A trust containing the assets of a disabled A/R under age 65, which meets all of the following criteria, is not subject to consideration as an available resource or as a resource disposed if:

- The trust was established by one of the following:
 - a parent;
 - a grandparent;
 - a legal guardian;
 - a court; and
- the trust contains the provision that, upon the death of the A/R, the amount remaining in the trust will reimburse the State for all Medical Assistance payments made on behalf of the A/R; and
- the trust was established for the sole benefit of a person who:

- is under 65 old; and
- is considered disabled as per COMAR 10.09.24.02B (19).

When a trust is established for a disabled individual under age 65, the exception for the trust discussed above continues even after the individual becomes age 65 as long as the individual continues to be disabled as defined by SSI. However, such a trust cannot be added to or otherwise augmented after the individual reaches age 65. Any such addition or augmentation after age 65 will be treated as a transfer of assets for less than fair market value.

The disability of the person for whom the trust is established must be verified by receipt of SSA disability payments, SSI, or by the State Review Team (SRT).

The second criterion above is met only if the language of the trust is specifically approved in writing by the office of the Assistant Attorney General. Any trust that may be revoked or altered does not meet this criterion. It is the responsibility of the drafter of the trust to obtain this documentation prior to establishment of the trust. Any trust not accompanied by the approval of the Attorney General (AG) does not meet the necessary conditions and will be treated in accordance with all other provisions of OBRA '93. A trust is considered to be for the sole benefit of a disabled individual under age 65 if the transfer is arranged in such a way that no individual except that individual can benefit from the assets transferred in any way, either at the time of the transfer or at any time in the future. However, the trust may provide for reasonable compensation for a trustee or trustees to manage the trust.

If a beneficiary is named to receive the asset or whatever is left of it at the time of the individual's death, the transfer or trust will nevertheless be considered to have been made for the sole benefit of the individual, if the Maryland Medical Assistance Program is named as the primary beneficiary of the asset up to the amount paid for services provided to the individual, with the designated beneficiary or beneficiaries receiving any amount that remains.

(b) Trusts Established by Non- Profit Association

A trust which contains the assets of a disabled individual and which meets all of the following criteria is not subject to consideration as an available resource or as a resource disposed of.

- 1) The beneficiary (A/R) is a disabled persons as defined in COMAR 10.09.25.02B (19);
- 2) The trust is established by a non-profit association;

- 3) The trust is managed by the non-profit association;
- 4) A separate account is maintained for each beneficiary of the trust but the accounts are pooled for purposes of management and investment;
- 5) The accounts in the trust are established solely for the benefit of a disabled A/R by the disabled A/R or by a:
 - Parent;
 - Grandparent;
 - Legal guardian; or
 - Court; and
- 6) The trust contains the provision that, upon the death of the A/R, the amounts remaining in the A/R's account and not retained by the trust will reimburse the State for all Medical Assistance payments made on behalf of the A/R.

The second criterion above, non-profit status, must be verified by documentation submitted by the organization. The sixth criterion above is met only if the language of the trust is specifically approved in writing by the office of the Attorney General (AG). Any trust not accompanied by the AG's approval does not meet the necessary condition and will be treated in accordance with all other provisions of OBRA '93. It is the responsibility of the A/R to provide documentation of the non-profit status of the organization and the appropriate approval of the recovery provision.

While the provisions above are consistent with the federal code, COMAR goes on to introduce an very extensive list of provisions that must be included in each special needs trust document as a condition to considering it an exempt resource.

(c) Special Needs Trusts

As with any other trust, a special needs trust may only be considered a resource for the A/R if some or all of the funds going into the trust were from the resources or income of the A/R or the A/R's spouse. Also, it must meet the definition of a —resource., as being accessible to the A/R or the A/R's spouse. To be not countable as a resource, a Special Needs Trust established after August 10, 1993 must meet all the following criteria below in 1-11 (as specified in COMAR 10.09.24.08-2C):

1. The trust is irrevocable. Any trust that may be revoked or altered does not meet this criterion and so is counted as a resource.
2. The trust states that the beneficiary is disabled under COMAR 10.09.24.05E. The beneficiary's disability must be confirmed by the Social Security Administration

or by the State Review Team. If the beneficiary has not been determined disabled by SSA or SRT, the trust is counted as a resource.

3. The beneficiary of the trust is younger than 65 years old at the time of the trust is established. If the beneficiary was 65 or older when the trust was established, it is counted as a resource.
4. The trust was established by the beneficiary's parent, grandparent, legal guardian or a court. If the trust was established by any other person, it is counted as a resource.
5. The trust does not contain provisions that conflict with the policies set forth in COMAR 10.09.24.08-2. This means the trust must limit distributions to those that are for the sole benefit of the beneficiary. Also, no provision of the trust may thwart the Department's recovery, upon the death of the beneficiary, of Medical Assistance benefits paid on behalf of the beneficiary. If the trust conflicts with these policies, it is counted as a resource.
6. The trust provides that the Department shall receive all amounts remaining in the trust upon the death of beneficiary, or upon termination of the trust of any other reason, up to an amount equal to the total Medical Assistance benefits paid on behalf of the beneficiary. If the trust does not provide for State recoveries, it is counted as a resource.
7. The trust does not permit distribution of trust assets upon termination of the trust that would hinder or delay reimbursement to the Department. Aside from distribution of administrative costs for termination of the trust, the Department must have first claim to the trust assets, up to the amount of Medical Assistance payments. If the trust permits distribution of its assets when it is terminated, it is counted as a resource.
8. The trust does not place time limits, or any other limits, on the Department's claim for reimbursement under COMAR 10.09.24.08-2C(8). If the trust places a limit on State recoveries, it is counted as a resource.
9. The trust must contain all of the following provisions:
 - a) Additions, including resources and income, may not be made to the trust after the beneficiary is 65 years old.
 - b) Expenditures from the trust must be used for the sole benefit of the beneficiary and must be directly related to the beneficiary's health care, education, comfort, or support.
 - c) The beneficiary may not serve as trustee or in any other capacity that would allow the beneficiary to influence or exercise authority or control over trust distributions.
 - d) The trustee must administer the trust in accordance with all of the following provisions of Estates and Trust Article § 15-502, Annotated Code of Maryland:

- The trustee may not have an interest in the trust's assets.
 - The trustee may not have discretion to use trust assets for the trustee's own benefit.
 - The trustee may not self-deal by selling trust assets to the trustee or buying trust assets from the trustee.
 - The trustee may not loan trust assets to the trustee.
- e) trustee must not take more compensation than is allowed in the provisions of Estates and Trusts Article, §14-103, Annotated Code of Maryland.
- f) Any leases or mortgages that the trust holds must contain a provision that they either terminate or become due and payable when the beneficiary dies or the trust is terminated.
- g) If the trust owns titled property that is valued at more than \$500.00, the property must be titled to the trust, except for securities which may be held in the name of a nominee.
- h) If the trust owns an asset jointly with another, the ownership must be as tenants in common and the ownership agreement must provide that, when the trust is terminated, the property must be sold for fair market value or the other owners must purchase the trust's interest in the property for fair market value.
- I) Trust assets may not be held as an ongoing business or enterprise, or as investments in new or untried enterprises.
- j) Trust distributions may not be used to supplement Medical Assistance payments to any health care provider serving the beneficiary. The provider is required to accept Medical Assistance reimbursement as payment in full for the services billed.
- k) Trust assets may not be used to compensate family members of the beneficiary for serving the beneficiary in any way, including:
- Caring for the beneficiary;
 - Accompanying the beneficiary on travel;
 - Providing companionship to the beneficiary; or
 - Serving as trustees or on a trust advisory committee.
- l) Trust assets may not be used to purchase gifts.
- m) Trust assets may not be used to purchase a life insurance policy on the life of the beneficiary.
- n) Trust assets may only be used to purchase a life insurance policy on the life of someone other than the trust beneficiary if the trust is the only beneficiary of the life insurance policy.

- o) Trust assets may not be used to purchase an annuity on the life of the beneficiary, unless the annuity provides that:
 - The final payment to the trust must be made before the beneficiary is 65 years, and
 - If the beneficiary dies before the final payments have been made, the remaining payments must be paid directly to the State until the total Medical Assistance benefits paid on behalf of the beneficiary have been reimbursed.
- p) The trust may not loan trust assets without security, which may include an ownership interest in real or personal property of at least equivalent value.
- q) The trust may only make loans if the loan agreement provides for immediate repayment in the event of the death of the beneficiary or termination of the trust for any other reason
- r) The only real property in which the trust may invest is in a single home property, which is used as the residence of the beneficiary and is titled in the name of the trust. The trust may not disburse more than \$100,000.00 for the purchase of property, without the approval of the State circuit court in the jurisdiction where the beneficiary lives.
- t) An annual accounting of the trust, including a listing of current assets, income and itemized distributions in the previous year must be sent to:

DHMH Maryland Medical Assistance Program
Division of Recoveries and Financial Services
201 W. Preston Street, 2nd Floor
Baltimore, Maryland 21201

- u) Trust assets may not be used to pay funeral expenses of the beneficiary, but may be used to purchase an irrevocable burial contract for the beneficiary to cover the beneficiary's future funeral and burial expenses.
- v) The trust may not receive payments from an annuity or a structured settlement that may provide lump sum or periodic payments, unless the annuity or settlement provides that:
 - The final payment to the trust is received before the beneficiary is 65 years old; and
 - If the beneficiary dies before the annuity or settlement is fully paid, the balance shall be paid directly to the State until the total Medical Assistance benefits paid on behalf of the beneficiary have been reimbursed.

If the trust does not contain all of these provisions or violates any of them in any way, it is counted as a resource.

10. If any amendments are made to the trust, the amendments must comply with COMAR 10.09.24.08-2 and a copy of the amendments must be sent for review to the DHMH Division of Recoveries and Financial Services; and

11. If the trust agreement fails to comply with any provision of COMAR 10.09.24.08-2, the full value of the assets in the trust must be considered available and countable resources of the trust beneficiary for the purpose of Medical Assistance eligibility determination.

2. Sole Benefit Definition

800.22 Sole Benefit

A transfer or trust is considered to be for the sole benefit of the A/R's spouse, the A/R's blind or disabled son or daughter, or a disabled individual under age 65 if the transfer is arranged in such a way that no individual or entity except the spouse, child, or disabled individual can benefit from the assets transferred in any way, whether at the time of the transfer or at any time in the future. A transfer or trust that provides for funds or property to pass to a beneficiary other than the spouse, blind or disabled child, or non-elderly disabled individual is not considered to be established for the sole benefit of one of these individuals.

E. New Jersey - a 1634 State

The state agency responsible for administering Medicaid in New Jersey is the Department of Human Services, Division of Medical Assistance and Health Services (DMAHS). Like Maryland, New Jersey has also added extensive conditions to the plain language of 42 U.S.C. §1396p(d). The rules for special needs trusts and pooled trusts are found in the New Jersey Administrative Code, beginning in paragraph (g) of §10:71-4.11, Trusts.

(g) The trust provisions shall not apply to the following trusts so long as the trust document meets all the requirements set forth in this chapter:

1. A special needs trust, that is, a trust containing the assets of a disabled individual and which is established prior to the time the disabled individual reaches the age of 65 and which is established for the sole benefit of the disabled individual by a parent, grandparent, legal guardian of the disabled individual or a court, may be excluded from the rules regarding the treatment of a trust.

To qualify for the exclusion, the trust shall contain the following provisions:

I. The trust shall be identified as an OBRA '93 trust established pursuant to 42 U.S.C. § 1396p(d)(4)(A).

(1) The trust shall not contain any provisions intended to give anyone or a court the power to alter the form of the trust from an individual trust to a "pooled trust" under 42 U.S.C. § 1396p(d)(4)(C). Notwithstanding amendments to the trust solely to conform to the requirements of this subsection and/or 42 U.S.C. § 1396p(d)(4), there shall be no provisions permitting the trust to be altered for any other reasons.

ii. The trust shall specifically state that the trust is for the sole benefit of the trust beneficiary.

(1) Only trusts which are intended for the sole benefit of the disabled individual are special needs trusts. Any trust which provides benefits to other persons shall not be considered an individual special needs trust. If expenditures are made from the trust which shall also incidentally provide an ongoing and continuing benefit to other persons, those other persons who also benefit shall contribute a prorata share to the trust for the subsequent expenses associated with their use of the acquisition,

(A) For example, if the trust acquires housing for the benefit of the trust beneficiary, and other family members also live in that house, the trust document shall provide that the trustee shall require and collect a pro rata contribution for the expenses of uses incurred, and shall return such contribution to the trust. Such collections shall be reflected in the annual required trust accounting. Any property acquired by the trust shall be titled solely in the trust's name. In addition, unless the trust is given equity in any improvements to real property, the trust shall not pay for upkeep, property taxes or other expenses associated with the property or any additions to the existing property.

iii. The trust shall specifically state that its purpose is to permit the use of trust assets to supplement, and not to supplant, impair or diminish, any benefits or assistance of any Federal, State or other governmental entity for which the beneficiary may otherwise be eligible or which the beneficiary may be receiving.

(1) If the trust provides for food, clothing or shelter, such expenditures shall be considered income under Social Security and Medicaid eligibility rules.

(2) It may be permissible for the trust to acquire property which is used to provide shelter for the trust beneficiary, but the trustee shall take care to ensure that such acquisitions do not create unintended problems (such as disqualifying someone for Federal benefits). Additionally, parents shall not be relieved of their duty to support their minor child, if they are capable of doing so. A minor's funds in a trust shall not be expended on routine support, unless the parents' income is insufficient for these expenses. N.J.S.A. 3B:12-43.

iv. The trust shall specifically state the age of the trust beneficiary, that the trust beneficiary is

disabled within the definition of 42 U.S.C. § 1382c(a)(3) and whether the trust beneficiary is competent at the time the trust is established.

(1) If the trust beneficiary is a minor, the trustee shall execute a bond to protect the child's funds or shall get a court's permission not to do so.

(2) If there is some question about the trust beneficiary's disability, independent proof may be required.

(3) If the trust beneficiary is a minor, the trust shall state whether the trust beneficiary is expected to be competent at his or her majority.

v. The trust shall specifically identify, in an attached schedule, the source of the initial trust property and all assets of the trust. If the trust is being established with funds from the proceeds of a settlement or judgement subsequent to the bringing of a legal cause of action, Medicaid's claim for its expenditures that are related to the cause of action shall be repaid immediately upon the receipt of such proceeds and prior to the establishment of the trust.

(1) Subsequent additions made to the trust corpus shall be reported to the appropriate eligibility determination agency. Subsequent additions to the trust (other than interest on the corpus) shall cease when the trust beneficiary reaches age 65, or shall be subject to transfer provisions.

(2) If subsequent additions are to be made to the trust corpus with funds not belonging to the trust beneficiary, it shall be understood that those funds are a gift to the trust beneficiary and cannot be reclaimed by the donor.

vi. If the trust makes provisions which are intended to limit invasion by creditors or to insulate the trust from liens or encumbrances, the trust shall state that such provisions are not intended to limit the State's right to reimbursement or to recoup incorrectly paid benefits.

vii. The special needs trust shall state that it is established by a parent, grandparent, or legal guardian of the trust beneficiary, or by a court.

(1) The trust shall identify the grantor/settlor by name and as the parent, grandparent, legal guardian, or court. A court can be named as the grantor, if the trust is established pursuant to a settlement of a case before it, or if the court is otherwise involved in the creation of the trust.

viii. The trust shall specifically state that it is irrevocable. Neither the grantor, the trustee(s), nor the beneficiary shall have any right or power, whether alone or in conjunction with others, in whatever capacity, to alter, amend, revoke or terminate the trust or any of its terms or to designate the persons who shall possess or enjoy the trust estate during his or her lifetime.

(1) Notwithstanding the irrevocability provision above, the trust can state that "the trust shall be irrevocable except that the trust may be amended as necessary to conform with the requirements of 42 U.S.C. 1396p and/or state law."

ix. The trustee shall be specifically identified by name and address. The trust shall state that the original trust beneficiary cannot be the trustee. The trust shall make provisions for naming a successor trustee in the event that any trustee is unable or unwilling to serve. The Bureau of Administrative Control, Division of Medical Assistance and Health Services, as well as the trust beneficiary and/or guardian, shall be given prior notice if there is a change in the trustee.

x. The trust shall specifically state that the trustee shall fully comply with all State laws, including the Prudent Investor Act, N.J.S.A. 3B:20-11.1 et seq. The trust shall provide that the trustee cannot take any actions not authorized by, or without regard to, State laws. If the trust gives the trustee authorization or power not provided for in the Prudent Investor Act, an accompanying letter shall provide an explanation for each such authorization or power.

xi. Except as approved by court order, after notice to the Division of Medical Assistance and Health Services, individual trustee fees shall be in accordance with N.J.S.A. 3B:18-23 et seq. or, in the case of a corporate trustee, the corporate trustee's regular fee schedule. The trustee shall not delay or defer accepting compensation or commissions more than one year from the date(s) they would otherwise be payable under the terms of the trust or of any applicable statute or rule. If the trust identifies a guardian, the trust shall specifically identify him or her by name. A guardian shall be compensated only as provided by law. The parent of a minor child shall not be compensated from the trust as the child's guardian.

(1) If an adult beneficiary is not competent, the trust shall specifically state that the "guardianship protections for the incompetent's funds which are required by New Jersey law and Court rules are incorporated by reference into this trust." The trustee shall either file a bond or shall get the Court's permission not to do so.

xii. The trust shall specifically state that, upon the death of the primary beneficiary, the State will be notified, and shall be paid all amounts remaining in the trust up to the total value of all medical assistance paid on behalf of the beneficiary. The trust shall comply fully with this obligation under the statute to first repay the State, without requiring the State to take any action except to establish the amount to be repaid. Repayment shall be made to the Treasurer, State of New Jersey, and shall be sent to the Division of Medical Assistance and Health Services, to the attention of the Bureau of Administrative Control, PO Box 712, Trenton, New Jersey 08625-0712, or to any successor agency.

xiii. If there is a provision for repayment of other assistance programs, the trust shall specifically state that the Medicaid Program shall be repaid prior to making repayment to any other assistance programs.

xiv. The trust shall specifically state that if the beneficiary has received Medicaid benefits in more than one state, each state that provided Medicaid benefits shall be repaid. If there is an insufficient amount left to cover all benefits paid, then each state shall be paid its proportionate share of the amount left in the trust, based upon the amount of support provided to the beneficiary.

xv. No provisions in the trust shall permit the estate's representative to first repay other persons or creditors at the death of the beneficiary. Only what remains in the trust after the repayments specified in (g)lxii, xiii and xiv above have been made shall be considered available for other expenses or beneficiaries of the estate. The trust may provide for a prepaid burial plan, but shall not state that it will pay for reasonable burial expenses after the death of the trust beneficiary.

xvi. The trust shall specify that a formal or informal accounting of all expenditures made by the trust shall be submitted to the appropriate eligibility determination agency on an annual basis.

xvii. The State shall be given advance notice of any expenditure in excess of \$ 5,000, and of any amount which would substantially deplete the principal of the trust. Notice shall be given to the Division of Medical Assistance and Health Services, Bureau of Administrative Control, PO Box 712, Mail Code 6, Trenton, New Jersey 08625-0712, or any successor agency, 45 days prior to the expenditures.

xviii. New Jersey rules and laws do not permit a trust to create a will for an incompetent or a minor. The money creating the trust, any additions and/or interest accumulated, cannot be left to other parties, but shall pass by intestacy. The trust shall not create other trusts within it.

2. A pooled trust is a special needs trust, containing the assets of a disabled individual, which meets the following conditions:

I. The trust shall be established and managed by a non-profit association;

ii. A separate account shall be maintained for each beneficiary of the trust, but for purposes of investment and management of the funds, the trust may pool the funds from those accounts;

iii. Accounts in the trust shall be established solely for the benefit of the disabled individual by the individual, by a parent, grandparent, or legal guardian of the individual, or by a court;

iv. To the extent that amounts remaining in the beneficiary's account upon the death of the beneficiary are not retained by the trust, the trust shall pay to the State of New Jersey the amount remaining in the account, up to an amount equal to the total amount of medical assistance paid under Title XIX of the Social Security Act on behalf of the individual. To meet this requirement, the trust shall include a provision specifically providing for such payment; and

v. Funds of an individual 65 or older, which are transferred to a pooled trust shall be subject to the transfer penalty provisions contained in N.J.A.C. 10:71-4.10.

2. Sole Benefit Definition

N.J.A.C. § 10:71-4.10 Transfer of assets, paragraph (b)8.

8. In order for a transfer of assets to be considered to be for the sole benefit of a spouse, disabled child or disabled individual under the age of 65, for the purposes of this subchapter, the transfer shall have been arranged in such a way that no individual except the spouse, disabled child or disabled individual under age 65 can, in any way, benefit from the assets transferred either at the time of the transfer, or at any time in the future. For the purpose of this subchapter, the person administering the funds shall only be compensated for the reasonable costs that can be directly attributable to the administration of the funds and for compensation for that administration. In no event shall such compensation exceed the amounts allowed by law for the administration of trusts. The transfer of asset penalty exemption for transfers made for the sole benefit of the spouse, disabled child or disabled individual under the age of 65 does not impact the treatment of a trust pursuant to N.J.A.C. 10:71-4.11.

F. Ohio - a 209(b) State

The state agency responsible for administering Medicaid in Ohio is the Ohio Department of Medicaid (ODM). Ohio's trust rules are contained in both the Ohio Revised Code and in the Ohio Administrative Code. Because there is only slight variation between these two sets of rules, only the Administrative Code provisions are reproduced below.

1. Trust Rules

Ohio Administrative Code, 5160:1-3-27.1, (C)(3)(a) and (c).

(3) Category three: exempt trusts. The principal or income from any one of these trusts is exempt from being counted as a resource.

(a) Special needs trusts are not countable resources. A trust qualifies as a special needs trust if the following conditions are met.

(I) The trust contains the assets of an individual under age sixty-five. The trust may also contain the assets of other individuals.

(ii) The individual is disabled as defined in rule 5101:1-39-03 of the Administrative Code.

(iii) The trust is established for the benefit of the individual by a parent, grandparent, legal guardian, or a court.

(iv) The trust requires, upon the death of the individual, the state will receive all amounts remaining in the trust, up to an amount equal to the total amount of medical assistance paid on behalf of the individual.

(v) When such a trust was established for a disabled individual under age sixty-five, the exception for the trust continues even after the individual becomes age sixty-five, provided the individual continues to be disabled as defined in rule 5101:1-39-03 of the Administrative Code. However, with the exception of income earned by the trust, such a trust cannot be added to or otherwise augmented after the individual reaches age sixty-

five. Any such addition or augmentation by the individual, with his or her own assets, after age sixty-five is treated as a transfer of assets subject to the rules prohibiting the improper transfer of resources.

(vi) Cash distributions to the individual are counted as unearned income. All other distributions from the trust are treated under the rules governing in-kind income.

(vii) Transfers of assets to a special needs trust are not subject to the improper transfer provisions in rule 5101:1-39-07 of the Administrative Code. However, assets held prior to the transfer to this trust are countable assets and/or income.

(c) Pooled trusts are not countable resources. A trust qualifies as a pooled trust only under all of the following conditions.

(I) The trust contains the assets of an individual of any age who is disabled as defined in rule 5101:1-39-03 of the Administrative Code.

(ii) A separate account is maintained for each beneficiary of the trust but, for purposes of investment and management of funds, the trust pools the funds in these accounts.

(iii) Accounts in the trust are established by the individual, the individual's parent, grandparent, or legal guardian, or a court solely for the benefit of individuals who are disabled.

(iv) To the extent that any amounts remaining in the beneficiary's account upon the death of the beneficiary are not retained by the trust, the trust pays to the state the amount remaining in the account equal to the total amount of medical assistance paid on behalf of the beneficiary. To meet this requirement, the trust must include a provision specifically providing for such payment.

(v) Cash distributions to the individual are counted as unearned income. All other distributions from the trust are treated under the rules governing in-kind income.

(vi) Transfers of assets to a pooled trust are not subject to the improper transfer provisions in rule 5101:1-39-07 of the Administrative Code. However, assets held prior to the transfer to this trust are countable assets and/or income.

2. Sole Benefit Definition

Ohio Administrative Code at Chapter 5160:1-3-07

(F) As used in this rule, a "transfer for the sole benefit" is a transfer that cannot, under any circumstance, benefit any individual or entity except the spouse, blind or disabled child, or disabled individual, at the time of the transfer or at any time after the transfer.

G. South Carolina - a 1634 State

The state agency responsible for administering Medicaid in South Carolina is the Carolina Department of Health and Human Services (SCDHHS). The state's Medicaid eligibility rules are found in its Medicaid Policy and Procedures Manual. For certain portions of its Manual, it has separate but nearly identical provisions for a strict policy and a liberalized policy. The trust provisions are identical in each version, and the differences between these two policies is not relevant to this paper. The policy provisions reproduced below are taken from the liberalized policy.

302.30.06 Special Needs Trusts

This type of trust is designed especially for individuals under the age of 65 who meet the SSI definition of disability. Special Needs Trusts established for a disabled individual age 64 or younger are exempt from the application of the transfer of assets penalty provision. Therefore, funds placed in a Special Needs Trust established for an individual age 65 or older will be subject to a penalty for a transfer of assets for less than fair market value. Further, once an individual reaches age 65, any funds or assets placed into the trust will be considered a transfer, even if the trust was properly established by a disabled individual age 64 or younger.

Criteria

- Established for the sole benefit of the disabled individual by:
 - Parent
 - Grandparent
 - Legal Guardian
 - Court
 - Must be funded initially with the income and/or resources of the disabled individual
- Note: Assets from any individual may be placed in the trust after the initial funding.
- Must contain a provision stating that at the individual's death, the state will receive all amounts remaining in the trust up to the amount expended by Medicaid on the individual's behalf.
 - Some Special Needs Trusts have a provision allowing the trustee to make loans from the trust. On or after September 1, 2003, any loan provision must be accompanied by a requirement that the trustee furnish SCDHHS with documentation of the following:
 - Source of the payback funds
 - An amortization schedule (schedule of the monthly payments of principal and interest)
 - Must have a reasonable rate of interest

- Must be actuarially sound (that is, expected to be paid back during the person's life expectancy).
 - o Documentation must be provided prior to funds being disbursed for the loan.
 - o Loans made that do not meet the above requirements are counted as income in the month received.
- May be established with the individual's income.
 - o The income must belong to the individual and be placed in the trust after he or she has received it.
 - o Income that is placed in the trust is not counted when determining the individual's Medicaid eligibility. Any income, including Social Security Benefits, VA pensions, private pensions, can be placed directly in the trust by the applicant/beneficiary without it affecting the individual's Medicaid eligibility. Also any income generated by the trust, which remains in the trust, is not counted as income.
 - o Any payments paid by the trust directly to the individual are counted as income for eligibility purposes.
 - o Any payments made by the trust to purchase food or shelter for the individual is considered as in-kind income for eligibility purposes.

302.30.07 Pooled Trusts

Pooled trusts contain the assets of individuals who meet the SSI definition of disability. Although a pooled trust may be established for beneficiaries of any age, only trusts established for a disabled individual age 64 or younger are exempt from the application of the transfer of assets penalty provision. Therefore, funds placed in a pooled trust established for an individual age 65 or older will be subject to a penalty for a transfer of assets for less than fair market value. Further, once an individual reaches age 65, any funds or assets placed into the trust will be considered a transfer, even if the trust was properly established by a disabled individual age 64 or younger.

Criteria

In order for such a trust to be exempt from the transfer of assets penalty, the trust must:

- Be established and managed by a non-profit association
Example: Babcock Center
- Have a separate account maintained for each beneficiary
- Contain an account in the trust solely for the benefit of the disabled individual which is funded by the disabled individual, parent, grandparent, legal guardian or court; and
- Contain a provision stating that at the individual's death, the state will receive all amounts remaining in the individual's account up to the amount expended by Medicaid on the individual's behalf.

Although an account is established for each member of the pooled trust, funds in the trust are pooled for investment and management purposes.

2. Sole Benefit Definition

The author was unable to find a definition for sole benefit in either the strict or liberalized resource sections of the South Carolina Medicaid Policy and Procedures Manual.

H. Texas - a 1634 State

The state agency responsible for administering Medicaid in Texas is the Health and Human Services Commission (HHSC). Chapter 358 of the Texas Administrative Code contains a high amount of detail about Medicaid policy in Subchapter C, but it does not provide detail on special needs trusts and pooled trusts. However, this detail is found in the HHSC Medicaid for the Elderly and People with Disabilities Handbook

1. Trust Rules

F-6710 Special Needs Trust

A special needs trust is a revocable or irrevocable trust established with the assets of a person under age 65 who meets the SSI program's disability criteria. The trust must be established for the person's benefit by his parent, grandparent, legal guardian or a court. The trust must include a provision that the state is designated as the residuary beneficiary to receive, at the person's death, funds remaining in the trust equal to the total amount of Medicaid paid on his behalf.

Use Form H1210, Subrogation (Trusts/Annuities/Court Settlements), to report to the Provider Claims Payment Section any potential paybacks to the state as the residuary beneficiary of special needs trusts. This trust exception continues even after a person becomes age 65 if he continues to meet the disability criteria for the SSI program. However, additions or augmentations to the trust after the person becomes age 65 are a transfer of assets.

If a person currently is receiving disability benefits from SSI, RSDI or Railroad Retirement (RR), his disability is automatically established. Verify that the SSI, RSDI or RR benefit is a disability benefit. Otherwise, disability must be established.

F-6720 Pooled Trust

A pooled trust is a revocable or irrevocable trust containing the assets of a person who meets SSI's definition of disability and which satisfies the following conditions:

- It was established and is managed by a non-profit association.
- A separate account is maintained for each beneficiary but, for investment and management purposes, the accounts may be pooled.
- Accounts in the trust are established solely for the benefit of persons who

meet SSI's disability criteria, and the trusts are established by a parent, grandparent or legal guardian of such individuals by a court, or by the disabled individuals themselves.

- The trust must include a provision that, to the extent that amounts remaining in a person's account at his death are not retained by the trust, the state is reimbursed in an amount equal to the total amount Medicaid paid on the person's behalf.

Note: Use Form H1210 to report to the Provider Claims Payment

2. Sole Benefit Definition

Chapter I-1100 of the Medicaid Manual and Subchapter C, Division 4, of the Administrative Code closely track the federal code on the transfer of assets, but neither the Manual nor the Code provide a definition for “the sole benefit.” Texas also has three unusual but beneficial statutes that can aid in the establishment of special needs trusts.²⁶

CONCLUSION

This paper began with a statement that the sole benefit rule is both the touchstone and the bane of special needs trust practitioners and trustees. One qualifier should be added to this statement regarding trustees in that it only applies to professional trustees who understand and appreciate the complexities that can arise in their efforts to comply with the rule. However, whether we consider the attorney or the trustee, it is the obvious responsibility and duty of the professional to rise to the challenge of these complexities. It is the professional who must guide the trust beneficiary through the quagmire of the SSI and Medicaid eligibility rules by making sure the trust is drafted and administered so it complies with all the applicable rules.

As the touchstone for practitioners, the sole benefit rule serves as a primary drafting objective while balancing other prudent and necessary trust objectives. The rule can also be the bane of practitioners because of the inherent tension between the interests of the client, or trust beneficiary, and the interests of the reviewing agency. On one hand, the client naturally wants the trust to be as flexible and beneficial as possible, while, on the other hand, the agency wants

²⁶ In the settlement of lawsuits, Section 142.005(a) of the Texas Property Code grants courts the authority to create trusts for minors who do not have legal guardians and for incapacitated people who are represented by a next friend or guardian ad litem. The statute requires such a court created trust to contain certain provisions for the protection of the trust beneficiary, but sub-paragraph (g) allows for the creation of a special needs trust. In addition, Section 1301 of the Estates Code allows Texas courts to create management trusts upon petition for the protection of Wards. Section 1301.101 includes a list of terms that management trusts must include, which would seem to preclude the creation of a special needs trust. However, sub-paragraph (c) of Section 1301.101 also gives the court discretion to omit or modify these required terms, and Section 1301.102 grants discretion to the court to add terms. Both of these provisions would allow for the possibility of a special needs trust. A similar provision is found in Section 1302.001 that authorizes courts to create pooled trust sub-accounts upon the petition of a guardian, an ad litem, or the individual with a disability who will be the trust beneficiary.

the trust to be as inflexible and restrictive as possible. Based on some of the state sampling in the section above, it would not be unreasonable to conclude that some agencies design their rules to lock down trust funds for future recovery purposes.

As the touchstone for trustees, the sole benefit rule serves as the standard for evaluating and documenting trust disbursements. Each disbursement must result in the purchase of some service or product for the beneficiary, and each disbursement must have the appropriate documentation to support it. While this can be viewed as simply the discharge of a basic fiduciary duty, the sole benefit rule is often the bane of trustees because proper documentation can sometimes be a real struggle to obtain. This is because the trustee must connect all the dots so that an overworked SSI or Medicaid employee can easily determine that any given trust disbursement complied with the sole benefit rule without too much thought or analysis on the part of the agency employee.

Complying with the sole benefit rule requires the trustee to document that the trust beneficiary received all of the benefit and not just a benefit. This is not always as easy task when you consider that some agency workers have a bias against special needs trust beneficiaries and that not all special needs trust beneficiaries and their families demonstrate sterling standards of record keeping. Every special needs trust is different, but the trustee always needs to reconcile strict formality with some degree of flexibility. It is only through such a reconciliation that the trustee can protect the beneficiary's public benefits eligibility while also making sure the beneficiary receives some benefit from the trust.

Despite some of the logistical issues the sole benefit rule poses due to its restrictive nature, these extra restrictions can work to a beneficiary's best interests when they cause a trustee to consider its decisions and actions more carefully. The sole benefit rule can also provide natural protection against the influence of family members and newly found friends following the receipt of funds, and it can offer similar protection in guardianships. It provides this protection in both instances because, as the sole benefit rule dictates, a special needs trust is required by its terms to benefit no one but the trust beneficiary at the time the trust is established or at anytime during the beneficiary's lifetime.

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