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UNDERSTANDING SPECIAL NEEDS TRUSTS

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It's no secret. The cost of long-term care for seniors and persons with disabling conditions can be staggering. To pay for their care, people usually must either have private insurance, spend their own assets, rely upon family members or qualify for public benefits, most notably Medicaid. For all but a few, private insurance is out of the question. To be eligible for Medicaid, a person can only have limited assets. If an individual has too much, he won't qualify for public assistance. People with too many assets often end up paying for long-term care out of their own pockets, or those of their family members, until their money runs out, and they can qualify for Medicaid. With proper planning, it is possible for an individual to qualify for Medicaid while still preserving sufficient assets to pay for those things that may not be provided by public benefit programs. Using certain types of trusts, generally referred to as "Special Needs Trusts," the quality of life for individuals with disabilities can be raised. However, one must be careful to follow the rules when creating and implementing such trusts.

Under federal and state law, trusts which are established using the assets of a disabled individual, or those belonging to their spouse, are generally treated as available resources for Medicaid purposes. They must be used to pay for long-term care, goods and services, or "spent down," before that individual is eligible for Medicaid benefits. This rule applies to trusts established by the individual or spouse, or by any person acting with the authority or at the request of the individual or spouse. Such trusts affect Medicaid eligibility regardless of the purpose of the trust, the authority of the trustee to make discretionary distributions or restrictions on when or for what purpose distributions can be made. As a result, "trigger" trusts, or trusts that prohibit payment to or for the benefit of the individual who established the trust in the event he or she becomes disabled, are not permitted.

There are still some opportunities available to establish or maintain Medicaid eligibility using certain trusts, referred to as "Special Needs Trusts." These trusts are exceptions to the rules. Special Needs Trusts fall into two specific categories, depending upon whose money is used to fund the trust, either the "Self-Settled Special Needs Trust" or the "Third-Party Supplemental Needs Trust." As discussed below, each form has its own benefits and limitations, but the purpose of the trust is the same for both - to improve the quality of life of

individuals receiving public benefits by providing for their additional or special needs not available under the public benefit program. One must be careful, however, to follow the rules when creating and administering such trusts. When deciding which trust form to use, the threshold question that must be answered is simple. We must first ask, “Whose money is it?”

Self-Settled Special Needs Trusts: Notwithstanding any provision of law that would deem it an available resource, it is possible to establish an irrevocable trust using the assets of an individual with a disability and still be eligible for Medicaid. The trust must be created for the sole benefit of the person who is seeking public benefits by that individual’s parent, grandparent, or legal guardian or by a court. The beneficiary must be under 65 years old when the trust is established. There is no penalty for transferring the assets of the individual with the disability to the trust. The trust must provide that the State of Wyoming will be reimbursed for its Medicaid expenditures from any amounts remaining in trust on the death of the beneficiary.

The purpose for which the Self-Settled Special Needs Trust is intended is to supplement Medicaid, not supplant it. It is established to provide for the individual’s “Special Needs”. Trust funds can be spent for the disabled beneficiary’s extraordinary medical care, travel, entertainment and other benefits not provided through governmental programs. Care must be taken to control the availability of funds for the disabled individual’s support (i.e., shelter and food) to avoid the risk of eliminating the beneficiary’s eligibility for public benefits. The trustee must have complete discretion to make distributions and the disabled beneficiary cannot require or force the trustee to make a distribution.

Irrevocable Self-Settled Special Needs Trusts are frequently used for accident victims when there has been a recovery on a tort claim or an insurance settlement or when a disabled individual receives an inheritance. In such situations, if payments were made directly to the recipient of public assistance he or she would have more than the minimum allowable assets which would result in his or her loss of SSI and Medicaid benefits. With this type of trust excess assets can be sheltered and the beneficiary still qualify for Medicaid. The Self-Settled Special Needs Trust is a valuable tool to use in planning for the future needs of a disabled individual.

Third-Party Supplemental Needs Trusts: The Third-Party Supplemental Needs Trust is similar to the Self-Settled Special Needs Trust in many ways. This type of trust is frequently used by parents or grandparents who want to provide for a disabled child after he or she is gone. Like the Self-Settled Special Needs Trust, the purpose of the Third-Party Supplemental Needs Trust is to supplement public benefit programs, not supplant them. Again, care must be taken in drafting the trust instrument to ensure that funds can only be spent on goods and services not provided by governmental programs. Payments can only be made to third parties and the beneficiary cannot require that the trustee make a distribution. Because this trust is used to pay for additional benefits intended to improve the quality of the beneficiary’s life, the Third-Party Supplemental Needs Trust is sometimes called a “luxury trust.”

There are some critical differences between the Self-Settled Special Needs Trust and the Third-Party Supplemental Needs Trust. These differences stem from the answer to our original question, “Whose money is it?” Only assets belonging to the disabled beneficiary can be used to fund the Self-Settled Special Needs Trust. As the name implies, the Third-Party Supplemental Needs Trust is funded with money or assets belonging to someone other than the disabled beneficiary. These assets can be contributed by the individual’s parents, grandparents, aunts, uncles or anyone else who is concerned about the beneficiary. They can be in the form of cash, securities, life insurance or any other type of income producing property or assets that can be converted to income producing property. The important thing to remember is that none of the disabled individual’s assets can go into funding the trust.

Since none of the disabled beneficiary’s assets are used to fund the Supplemental Needs Trust, it is not subject to state or federal Medicaid law. There are no penalty periods applied for transferring assets. There is no requirement that the State be reimbursed. On the death of the beneficiary, any funds or assets remaining in the trust can be distributed to other persons such as an heir or entities like a charity. The Third-Party Supplemental Needs Trust can be either irrevocable or revocable. If the third-party who established the trust chooses to make it revocable, assets placed in trust can later be withdrawn and the trust terminated. Usually the Third-Party Supplemental Needs Trust is created while the third-party is still alive (inter vivos), but it can also be established under a Will (testamentary). If an inter vivos trust vehicle is used, the third-party or any other person can make transfers to fund the trust whenever they have a little extra cash on hand, or they can refer to the trust in their own Will without themselves incurring the cost of creating a trust.

Self-Settled Special Needs Trusts and Third-Party Supplemental Needs Trusts are valuable tools to be used in improving the quality of life and maintaining the dignity of an individual with a disabling condition. Often both types of trusts are used to address the long-term needs of the same individual. They do, however, require skillful drafting and a knowledge about how the trust interacts with the public benefit program for which the beneficiary is otherwise eligible. Anyone who is concerned about the future of a person with significant disabilities should consider incorporating a Special Needs Trust as part of his or her own estate plan.