

Settlement Proceeds and Special Needs Trusts FOR THE DISABLED

After litigating, negotiating, and settling a case for a disabled client, one hurdle may remain: creating a practical and successful settlement distribution plan. Because a client with disabilities may rely on government benefits for vital health insurance coverage and other essential needs, a settlement plan should protect your client's government-program eligibility and the corpus of the settlement award from being drained by private health care costs.

One way to do this is through a special needs trust. When considering one of these trusts for a disabled client, it is important to understand the differences between the two types of statutory trusts and examine their advantages and disadvantages.

Federal government assistance programs, such as Medicaid, supplemental security income,¹ the U.S. Department of Agriculture's supplemental nutrition assistance program,² and the U.S. Department of Housing and Urban Development's affordable housing program,³ provide need-based benefits to people who meet eligibility criteria, including financial hardship tests. But without proper planning, distributing settlement proceeds to people receiving these benefits can be problematic.

For example, Medicaid provides health insurance benefits to certain people whose monthly income and assets fall within specific limits.⁴ Most state

If your client is disabled and receiving government benefits, a special needs trust may be a necessary component of settlement planning. But there are different types of trusts—each with its own pros and cons—that you must evaluate carefully.

By || **ANNIE K.T. WARNER**

Medicaid programs count lawsuit settlement proceeds as income for the month the funds are received and as an asset for each month thereafter. Distributing settlement proceeds directly to your client could elevate him or her above the income threshold for benefit eligibility and eliminate his or her government benefits, which can be devastating to a severely injured or disabled client. Without Medicaid, your client will be denied access to certain medical treatment and be forced to pay out of pocket for those services; the settlement proceeds will be exhausted, calling into question the settlement's overall benefit. But if the settlement funds are held in a special needs trust, they are not counted as income.

Protecting a client's benefits through settlement planning is important, and it falls under your ethical obligations of diligence and communication. Under ABA Model Rules 1.3 and 1.4, a lawyer must "act with commitment and dedication to the interests of the client"⁵ and "shall explain a matter to the extent reasonably necessary to permit the client to make informed decisions."⁶ You must have at least an awareness and basic knowledge of the settlement planning options available to a disabled client.

You have to supply your clients with the requisite information and accessibility to expert services to protect their government benefits. Before accepting a settlement, inform your client that his or her government benefits may be jeopardized by receipt of settlement proceeds. You should encourage your client to speak with the relevant government agencies (such as Medicaid or the Social Security Administration) regarding program financial eligibility parameters, as well as provide accessibility to a settlement planning or government benefit expert who can analyze benefits and viable settlement plan options. In meeting these ethical duties, you will enable your client to make an informed decision regarding the settlement plan; the client is protected, and you have limited your liability.

There are two types of special needs trusts: the pooled trust (d4c trust) and



the individual payback trust (d4a trust).⁷ Both protect your client's government-benefits eligibility while simultaneously allowing the funds to be used for supplemental needs—such as handicapped-accessible improvements or equipment—to improve his or her quality of life.

The two types of trusts differ in terms

of costs, establishment, and management. A d4a trust, or an individual payback trust,

- is created for disabled beneficiaries under age 65
- is established by a parent, grandparent, legal guardian, or court
- contains a payback clause to

reimburse the state, as first payee, for Medicaid benefits paid during the beneficiary's lifetime (including a provision apportioning payback among different states) to the extent that there are any remaining funds in the trust account

- is for the disabled beneficiary's sole

benefit during his or her lifetime. A d4c trust, also known as a pooled special needs trust,

- is created for disabled beneficiaries of any age
- is established and managed by a nonprofit organization or association
- contains the same payback clause to reimburse the state for Medicaid benefits
- is for the disabled beneficiary's sole benefit during his or her lifetime.

The beneficiary, a third party, or a court establishes the d4c's trust account, and a separate trust account is created for each individual beneficiary.

Although the statutory requirements are similar, the pooled special needs trust is the more user-friendly option when it comes to creation and cost. However, the individual payback trust offers some flexibility for those beneficiaries with large settlements and unique fund management concerns. When advising clients which type of special needs trust is best, consider the following factors.

Trust creation. An individual payback trust must be created for a person less than 65 years old by a third party, such as a parent, grandparent, legal guardian, or the court.⁸ The document creating the trust must be written by an attorney. With a disabled child or a minor beneficiary, finding a parent, legal guardian, or grandparent to create the trust may be easy, but what happens when a beneficiary has no such person to establish the trust? If this is the case, the court will establish it.

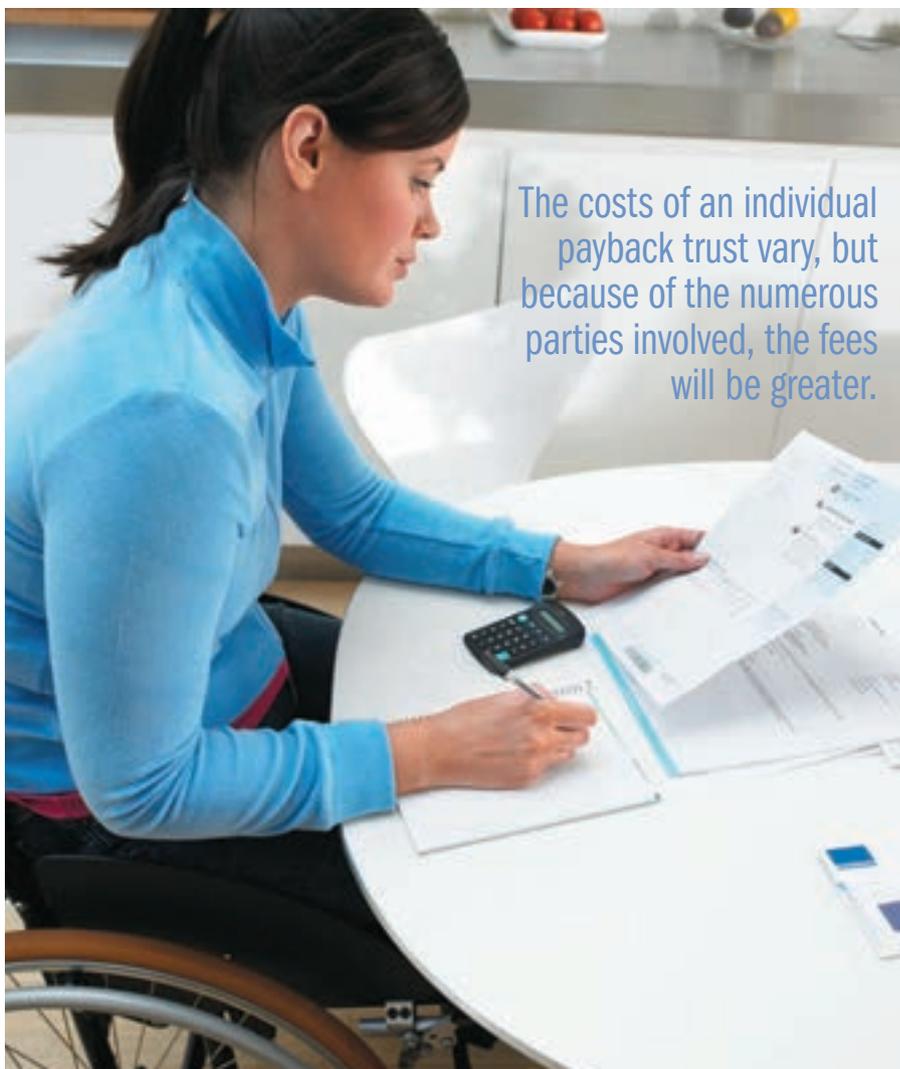
In contrast, a pooled special needs trust may be used for an individual of any age and can be created by either the beneficiary or a third party.⁹ This is an advantage, because there is no requirement to rely on a third party to create the trust account, and an attorney is not required to draft the trust document. Pooled special needs trust organizations

already have a master trust agreement (or declaration of trust) in place, which dictates the management and administration of the pooled trust accounts. Typically, the only written requirement is a joinder agreement: a fill-in-the-blanks document that may incorporate various trust provisions from the nonprofit organization's master trust or declaration of trust and that requires the beneficiary (or his or her guardian) to supply information regarding government benefits, remainder beneficiaries, and expected trust fund usage. The joinder agreement does not require an attorney's input, but you or an elder law attorney should review its provisions and help your client complete it.

Trust administration. With individual payback trusts, the beneficiary, his or her family, or an attorney will

select a trustee to manage and administer the trust's funds. This flexibility can be a comfort for the client who wants to ensure that the trustee is familiar and knowledgeable about his or her needs. The trustee must be well versed in government-benefits eligibility and have a working knowledge of permissible trust distributions to avoid running afoul of government agency regulations or losing these benefits. If an individual is selected as trustee, a local special needs attorney or government-benefits consultant should be retained to provide advice on permissible trust expenditures, changes in applicable regulations, and any tax or reporting requirements.

A pooled special needs trustee is the nonprofit organization that holds and administers the trust's accounts. Because the organization was created



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solely to manage the pooled trust funds, it possesses the requisite knowledge and experience. Although the beneficiary may not have an existing relationship with the trustee, the organization typically assigns an account representative or team to handle the beneficiary's distribution requests and care needs.

Cost considerations. Creating and administering a pooled special needs trust account is generally less expensive than an individual payback trust. A pooled special needs trust charges an initial joinder fee to establish the trust account, which ranges from \$500 to \$2,000 and may be based on a sliding scale determined by the amount deposited to fund the trust. For example, joinder fees for one national pooled special needs trust organization range from "free of charge," for trust accounts funded with \$2,500 or less, to its highest joinder fee of \$2,000 for trust accounts funded with \$40,000 or more, with several graduated fee tiers in between.¹⁰ There is also an annual administration fee that is either a flat fee or a percentage fee based on the trust account's principal. And if an elder law or trust attorney is hired to review the joinder agreement and assist with its completion, that attorney also may charge a fee.

The costs of an individual payback trust vary, but because of the numerous parties involved, the fees will be greater. Creation costs can include the trust attorney's fees (in drafting the trust documents), as well as potential court costs if no parent, grandparent, or guardian is available to establish the trust. A trust company or bank must administer and hold the trust account, and a separate trustee may have to manage the trust account—both of which involve costs. If a local special needs attorney or government benefit consultant is retained, their fees also must be factored in. And each party comes with his or her own fees and expenses—the trust attorney's

hourly rate, the trustee's annual or hourly fees, and the trust company or bank's expenses.

Financial resources. Pooled special needs trusts often are perceived as the option for beneficiaries with small amounts of money; individual payback trusts are considered a better vehicle for beneficiaries with significant resources. While it is true that a pooled special needs trust combines individual accounts within the trust and is an excellent trust device for smaller amounts, there are no monetary restrictions on how much can be contributed, making a pooled special needs trust a viable option for larger deposit amounts as well.

Conversely, to fund an individual payback trust, a beneficiary should have sufficient resources and/or unique planning needs, such as investment concerns or the need for flexible distribution procedures, to justify the costs associated with establishing and administering the private account.

Remainder beneficiaries. Both trusts allow the beneficiary (or his or her family) to name remainder beneficiaries to receive distributions after the beneficiary's death, should money be left over after the government is reimbursed for Medicaid services. When choosing a pooled special needs trust organization, the beneficiary must be aware that these organizations have the option of retaining the remainder of trust funds after the beneficiary dies. However, many pooled special needs trusts also allow the beneficiary to name a remainder beneficiary other than the trust organization, and provisions to this effect would be included in the joinder and master trust agreements.

While each type of special needs trust comes with its advantages and disadvantages, both can protect your disabled client's government-benefits eligibility and enhance his or her quality of life. You

MORE ON SPECIAL NEEDS TRUSTS

🔗 Visit the Web pages below for additional information.

AAJ SECTION

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must consider all these factors carefully when advising your client. 📄



Annie K.T. Warner is a managing member of Warner Ferris in Cincinnati. She can be reached at annie@warnerferris.com.

NOTES

1. See U.S. Soc. Sec. Admin., Supplemental Security Income Home Page, <http://ssa.gov/ssi>. Supplemental security income is a cash-assistance program for elderly, blind, and disabled individuals who meet certain financial eligibility tests.
2. See U.S. Dept. of Agric., Supplemental Nutrition Assistance Program (SNAP), www.fns.usda.gov/snap. SNAP offers food assistance to low-income people through state agencies.
3. The U.S. Dept. of Hous. & Urb. Dev., www.hud.gov. This agency offers federal assistance to low- and moderate-income people to help them find housing.
4. See Ctrs. for Medicare & Medicaid Servs., Medicaid and CHIP Program Information, www.medicaid.gov/Medicaid-CHIP-Program-Information/Medicaid-and-CHIP-Program-Information.html. Medicaid-eligible categories include children, adults, pregnant women, disabled people, seniors, and long-term care recipients.
5. Model R. Prof. Conduct 1.3 (ABA 2012).
6. Model R. Prof. Conduct 1.4 (ABA 2012).
7. Omnibus Reconciliation Act of 1993, 42 U.S.C. §1396p (d)(4)(A) & (C)(1993).
8. 42 U.S.C. §1396p (d)(4)(A).
9. 42 U.S.C. §1396p (d)(4)(C).
10. See Natl. Found. for Spec. Needs Integrity, Inc., Our Fees, www.specialneedsintegrity.org/our_fees.php.