

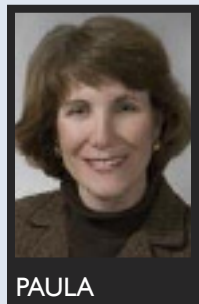


A primer on special needs trusts and their use

BY PAULA L. PEADEN

Special needs trusts (SNT) may be created when there is an inability of a beneficiary to manage funds due to a mental or physical incapacity, and/or where a beneficiary requires or may require government benefits, the qualification of which may be threatened by the beneficiary holding assets directly. Common governmental programs requiring the protection of an SNT are Supplemental Security Income (SSI) and Medicaid. Both of these programs are needs based and most SNT's are written to preserve both SSI and Medicaid. However, SNTs will vary depending on a client's individual needs.

As an attorney who has written thousands of estate plans, the most challenging and rewarding estate plans I work on are those with families that have a loved one with special needs. Many parents realize that as their children become adults they can no longer protect them in ways they could when their children were small and that their adult children will form decisions on their own. When the child is grown, the parents' job to provide such protection may be done, but the parents' concern for the child's well-being continues. As such, most parents' estate plans entrust their estate to their child, knowing that mistakes may and will happen, but in the end all will be well.



PAULA
PEADEN

Aging parents of a special needs child are not afforded the peace of mind that others enjoy; they cannot simply let go and believe that all will be well. The decisions to be made regarding how to leave an inheritance – "should all my children be treated equally or should my special needs child receive more or less"; "who will take care of my child well beyond their 18th birthday"; and "who should be the remainder beneficiary of the SNT" - are daunting.

Similarly, a caregiving spouse who spends day and night with their loved one, who may suffer from long standing mental illness, Alzheimer's, CVA etc., agonizes over how to leave their estate. Concerns, such as: "what will happen if I pass first"; "who will care for my spouse"; "where will my spouse live"; and "will my spouse be left penniless" can be somewhat relieved by the use of an SNT.

Special needs trusts are not only for planning for an inheritance or lifetime gift, but can also be used in a divorce situation where one of the children has special needs. Any life insurance ordered to be paid should generally be directed to an SNT, as payment to the individual could have negative ramifications with respect to qualifications for government assistance and services, as well as other concerns. Similarly, consideration should be given to assigning child support to an SNT for similar reasons.

Another area that requires special needs planning is working with litigators to protect settlements. It may be an accident, illness or malpractice that makes a person disabled. Settlements rarely can replace an individual's loss, but coordinating the set-



tlement proceeds with preserving or becoming eligible for government benefits provides a very important function for your client's needs. The SNT can be created to receive the settlement proceeds and assures that the beneficiary will not be barred from receiving government benefits to which they would otherwise be entitled. Many of these people will not have health insurance and can lose everything if a trust is not carefully crafted. Even those with health insurance and sizeable recoveries should have an SNT. The attorney should discuss an SNT to protect public benefits, as well as to protect the individual from squandering by relatives or friends of the client who may be unable to protect themselves. Do not assume that the client will not require public assistance. An SNT can be created at the time of settlement and any proceeds, including annuities can be assigned to the trust. Public benefit eligibility is important to preserve both small and large sums of money.

Below is a brief, non-exhaustive summary of common types of SNT's and how they may be used:

1. Stand alone SNT. Inter vivos stand alone trust which is typically funded by a parent or grandparent's revocable trust or last will and testament. It is referred to as a third party trust as it is established and funded with the assets of someone other than the beneficiary. At the beneficiary's death any remaining assets may pass to residuary heirs. Make sure other relatives know of this trust for gifts or inheritances, as it is generally preferable to have all such assets earmarked for the beneficiary to pass into the trust rather than into the beneficiary's direct possession and control;

2. Testamentary SNT. Frequently used by a spouse leaving funds for their surviving spouse who is or may be receiving Medicaid benefits. Virginia requires that a Medicaid recipient who is predeceased by a spouse assert their right to an elective share.

Any funds may be left to a spouse in an SNT, but it must be a testamentary trust contained in a will;

3. Pooled trust-Self-Settled SNT- Inter vivos pooled account trust established under 42 USC § 1396p(d) (4)(C). This trust is administered by a nonprofit association which acts as trustee. Assets are put into a master trust and a separate trust account is established for each beneficiary by the association. This trust may be used for smaller trust amounts and/or when the beneficiary wants to ultimately benefit the nonprofit association. It can only be done for those under 65. Transfer of assets to this trust does not penalize the beneficiary; and

4. Payback SNT- Established under 42 U.S.C. § 1396p (d) (4) (A) with the beneficiary's assets. This is considered a self-settled trust as this SNT contains the resources that have already vested in a beneficiary from an unplanned inheritance, lifetime gift, personal injury suit, malpractice suit or child support payments. This trust must have a mandatory Medicaid payback provision. It can only be done for those under 65. Transfer of assets to this trust does not penalize the beneficiary.

An SNT, while not a cure for all worries, can give families and beneficiaries some peace of mind. You can help your clients create an estate plan that will assure them that their loved one will continue with an advocate long past their death and insure that their loved one remains on or becomes eligible for government benefits while enjoying a good quality of life. Once your client understands how the government programs work and how the SNT will work, they will appreciate your guidance in creating a trust that will be their last act of protecting their loved one past their lifetimes.

Paula Peaden practices law with Parker, Pollard, Wilton & Peadon PC in Richmond.