

Presented:
Special Needs Trusts

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The “Dirty Dozen” Blatant Mistakes in SNTs

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I. Introduction

According to a study funded by the National Institute on Disability and Rehabilitative Research, it is estimated that over 48.9 million Americans are disabled. This number represents approximately 19.4% of the entire population of the United States. Of these individuals, one-half suffer from a severe disability.¹ The number of Americans with disabilities is expected to increase as the U.S. population ages. In light of the growing number of Americans with a disability, the need for special needs planning is growing.

Attorneys not familiar with special needs planning or attorneys just beginning to practice in this area, are often confused and overwhelmed with the vast amount of knowledge necessary to adequately advise and plan for their clients. While only one tool in the attorney's bag, special needs trusts present an excellent opportunity to preserve both assets and the beneficiary's eligibility for government benefits. However, improper drafting in the preparation of a special needs trust can create disastrous consequences for the beneficiary, including the reduction or total loss of means-tested government benefits.

This paper focuses on the top twelve drafting mistakes made during the preparation of special needs trusts. Part II of this paper gives a brief overview of both self-settled and third-party special needs trusts. Part III discusses the top twelve drafting mistakes in the preparation of special needs trusts.

I would like to acknowledge the attorneys and trust officers whose advice I solicited in the preparation of this presentation. These individuals include:

II. Special Needs Trust Overview

One of the most common tools used by attorneys in planning for government benefits is a special needs trust. Government benefits are designed to provide basic health care, food and shelter. As such, government benefits provide only a meager existence to recipients. A special needs trust is designed to provide the beneficiary with additional needs and extras, such as vacations, that normal government benefits do not provide. A special needs trust can either be self-settled or third-party settled depending on the source of funding. Each of these types of trusts are discussed below.

A. Self-Settled Special Needs Trusts

To provide for the payment of supplemental needs, federal law permits an individual with disabilities to retain his or her resources in one of two types of special needs trusts, without the creation of such trust or the value of the corpus of the trust,

¹ http://www.infouse.com/disabilitydata/disability/1_1.php.

disqualifying him or her from SSI² or Medicaid benefits.³ These two types of special needs trusts are self-settled or first-party trusts, meaning that these trusts are funded with the beneficiary's own funds.

1. (d)(4)(A) Special Needs Trust

A (d)(4)(A) special needs trust is a trust created (and funded) for the sole benefit of an individual with a disability under the age of 65 by the individual's parent, grandparent, legal guardian or court.⁴ The trust is funded with the individual's assets. The trust must provide that the state Medicaid agency will receive amounts remaining in the trust upon the individual's death up to the amount paid by each state under the Medicaid program for services to the individual.

2. (d)(4)(C) Pooled Special Needs Trust

A (d)(4)(C) special needs trust is a pooled trust created and managed by a nonprofit organization, such as the ARC of Texas. A separate subaccount is maintained for each beneficiary of the trust, but the assets are pooled for investment and management purposes. The subaccount is created for the sole benefit of an individual with a disability by the individual's parent, grandparent, legal guardian, court or the individual. The trust is funded with the individual's own assets. Some states, including Texas, require the (d)(4)(C) special needs trust be funded by the individual with disabilities prior to individual attaining the age of 65, otherwise any funding by the individual with disabilities with his or her own assets after that age may constitute a divestment by the individual and such divestment could result in a transfer of asset penalty.

The Association of Retarded Citizens ("ARC") has established a pooled trust that accepts contributions from persons residing anywhere in Texas. The ARC Pooled Trust provides professional management at less than the cost charged by many corporate trustees. Its effectiveness for sheltering certain assets has been pre-established by negotiation with the state Medicaid program – a process not available to individuals. And it does not require paying an attorney fee to establish the trust (although legal counsel is definitely needed to determine whether or not this is the best disposition of the assets to provide independent advice as to the alternatives).

To the extent the remainder may exceed reimbursements to Medicaid, the trust can pay the remainder to other designated beneficiaries (usually family members); and at the

² 42 U.S.C. §1382b.

³ 42 U.S.C. §1396p(d)(4).

⁴ 42 U.S.C. §1396p(d)(4)(A).

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