

12<sup>th</sup> Annual Changes and Trends Affecting  
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**How to Make a Trust a  
“Special Needs Trust”**

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# How to Make a Trust a “Special Needs Trust”

## Table of Contents

|      |                                                                                              |    |
|------|----------------------------------------------------------------------------------------------|----|
| I.   | First, A Primer on Trusts and Needs-Based Public Assistance. . . . .                         | 1  |
| A.   | What is a “Trust”? . . . . .                                                                 | 1  |
| 1.   | Definition of a Trust. . . . .                                                               | 1  |
| 2.   | Illustration. . . . .                                                                        | 2  |
| 3.   | There are five components to every trust. . . . .                                            | 2  |
| B.   | How Can a Trust Be Established?. . . . .                                                     | 4  |
| 1.   | Via a Last Will and Testament - A Testamentary Trust. . . . .                                | 4  |
| 2.   | Via a Separate Document - A Living Trust. . . . .                                            | 5  |
| 3.   | A Living Trust Can Be Revocable or Irrevocable. . . . .                                      | 5  |
| C.   | Whose Assets Are Being Held In Trust? Self-Settled v. Third<br>Party-Settled Trusts. . . . . | 5  |
| D.   | Which Distribution Standard Should Be Used?. . . . .                                         | 7  |
| E.   | What is Needs-Based Public Assistance?. . . . .                                              | 8  |
| F.   | What is the Purpose of a Special Needs Trust?. . . . .                                       | 8  |
| G.   | What Are the Requirements of a Self-Settled Special Needs Trust?. . . .                      | 9  |
| H.   | What Are the Requirements of a Third Party-Settled Special<br>Needs Trust?. . . . .          | 11 |
| II.  | Clauses That Need To Be In A Special Needs Trust. . . . .                                    | 12 |
| A.   | Settlor's Intent. . . . .                                                                    | 12 |
| B.   | Description of Type of Trust Being Established. . . . .                                      | 13 |
| C.   | Special Needs Distribution Standard. . . . .                                                 | 14 |
| D.   | Facility of Payment Clause. . . . .                                                          | 16 |
| E.   | Broad Trustee Discretion. . . . .                                                            | 16 |
| F.   | Broad Trustee Investment Powers. . . . .                                                     | 17 |
| G.   | Limits on the Trustee's Powers. . . . .                                                      | 18 |
| H.   | Limits on the Beneficiary's Powers. . . . .                                                  | 19 |
| 1.   | Power to Demand a Distribution from the Trust. . . . .                                       | 19 |
| 2.   | Power to Remove and Replace the Trustee. . . . .                                             | 20 |
| III. | Clauses to Consider Using in a Special Needs Trust. . . . .                                  | 20 |
| A.   | Power to Amend the Trust. . . . .                                                            | 20 |
| B.   | Oversight of the Trustee. . . . .                                                            | 22 |
| 1.   | Guardian or Conservator. . . . .                                                             | 23 |
| 2.   | Trust Protector or Trust Advisor. . . . .                                                    | 24 |
| 3.   | Personal Agent. . . . .                                                                      | 27 |
| C.   | Early Termination of the Trust. . . . .                                                      | 30 |
| 1.   | Early Termination of a Third Party-Settled Special Needs Trust. . . .                        | 31 |
| 2.   | Early Termination of a Self-Settled Special Needs Trust. . . . .                             | 32 |
| D.   | IRA Paying to a Special Needs Trust. . . . .                                                 | 33 |

|     |                                                                                                                |    |
|-----|----------------------------------------------------------------------------------------------------------------|----|
| IV. | Questions to Answer When Designing a Third Party-Settled<br>Special Needs Trust. . . . .                       | 36 |
| A.  | Should you use a Will with a Testamentary Trust or Living Trust?. . . .                                        | 36 |
| B.  | If Living Trust, Should it Be Standalone or a Section in Settlor's<br>Primary Revocable Living Trust?. . . . . | 37 |
| C.  | If Standalone Special Needs Trust, Should It Be Revocable<br>or Irrevocable?. . . . .                          | 40 |
| 1.  | Advantages of Revocable Standalone Special Needs Trust. . . .                                                  | 40 |
| 2.  | Disadvantages of Revocable Standalone Special Needs Trust. . .                                                 | 40 |
| 3.  | Advantages of Irrevocable Standalone Special Needs Trust. . . .                                                | 41 |
| 4.  | Disadvantages of Irrevocable Standalone Special Needs Trust. .                                                 | 41 |
| D.  | Is it better to write a trust in first person or third person perspective?. .                                  | 42 |
| V.  | And, In Conclusion. . . . .                                                                                    | 43 |

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A third party-settled special needs trust is nothing more than a traditional trust that directs the trustee to only distribute from the trust for the beneficiary’s “special needs”, preferably in a way that does not cause the beneficiary to lose or suffer a reduction in needs-based public benefits. Many provisions typically found in traditional trusts are either worded differently or eliminated in a special needs trust. And there are a few provisions that are typically only found in a special needs trust. In addition, if the special needs trust is self-settled, then it must strictly comply with federal law and should comply with administrative rules of the Social Security Administration and the agency administering the Medicaid program for the state where the beneficiary resides.

These materials will explain what the foregoing paragraph means and provide illustrations of clauses that are appropriate to use in a special needs trust. In order to help make this more understandable, we start with some very basic information about trusts and needs-based public assistance.

## I. First, A Primer on Trusts and Needs-Based Public Assistance

### A. What is a “Trust”?

**1. Definition of a Trust:** A trust is a legal arrangement under which one person or institution (Trustee) controls property given by another (Settlor/Grantor/Trustor) and uses it for the benefit of a third (Beneficiary). In other words, a trust separates **Legal Ownership** of property (which is given to the Trustee) from **Beneficial Ownership** (which is given to the Beneficiary).

A trust is a legal concept concerning how property is owned and managed. A trust itself cannot be seen or touched, but the property being held by the trustee in trust can.

**2. Illustration:** Normally, a person owns his or her property and can use the property as he or she deems appropriate. For example, if Billy owns a checking account that has money in it, then Billy can decide how to spend that money and can write checks at any time to spend the money however Billy wishes.

However, if that checking account is in a trust for Billy's benefit and someone other than Billy is the trustee of that trust, then it is the trustee, not Billy, who can write checks and spend the money. But, because Billy is the beneficiary of the trust, the money in the checking account can only be spent by the trustee in a manner that benefits Billy. There is a long history of cases and statutes that govern how a trustee must act. They hold the trustee to a fiduciary standard and require that the trust assets be handled prudently and in a manner that benefits the beneficiary.

**3. There are five components to every trust.** These are:

**a. Settlor (sometimes referred to as a Grantor or Trustor):** This is the person (or entity) who transfers assets belonging to him or her to the trustee to hold and use for the benefit of the beneficiary. This arrangement is called the "trust". Although often the settlor is also the person who signs a written document to establish the trust, this is not necessary. Merely transferring assets to a trustee is all that is required to make a person a "settlor".

**b. Trustee:** This is the person or entity (such as a corporate trust department or non-profit corporation) who holds the assets transferred by the settlor and distributes those assets, or the income earned by investing those

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