

TRUST REFORMATION IN TEXAS

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I. Introduction

An attorney who works with clients who receive Supplemental Security Income or Medicaid understands the importance of special needs trusts. We spend a significant amount of time counseling our clients and their families about the importance of asset preservation, trusts, and eligibility for public benefits. Sometimes we find, even after all of our hard work and counseling, that a well-meaning family member or friend has named our client as Beneficiary of a trust that does not meet the requirements of a special needs trust.

Upon such a discovery, we might sort through the following decision tree: if the Beneficiary is under age 65, a special needs trust could be created and the assets from the well-intended family member could be placed in the special needs trust. The procedure to be followed would differ depending upon whether the person is a competent adult or a minor, whether the individual has a living parent or grandparent, and some other specific facts of the situation. The creation of a special needs trust would not be the only methodology that could be used to maintain the eligibility of the person, but it has been and remains a popular and effective strategy.

Another—very attractive—alternative can be found in the new section of the Texas Estates Code—section 112.054. A copy of the section is attached as “Exhibit A” to this paper. This section of the Texas Estates Code allows for judicial modification or reformation of a trust. The salient part of the statute, for our discussion, is the section of the new law that specifically authorizes the reformation of a trust to qualify a distributee for government benefits.

In the example above, a possible strategy would be to reform the existing trust so that the asset(s) flow(s) into a special needs trust for the person receiving benefits. Doing so would prevent the asset from being considered an available resource that would disqualify the individual for the benefits of a means-tested program like Social Security Income or Medicaid. The process would likely save time when compared to petitioning a court to create a special needs trust under Section 1301 of the Estates Code and

would likely provide additional benefits.

This paper addresses, specifically, the reformation of a trust such that it creates a special needs trust for the benefit of a Beneficiary. While there may be other ways to reach the desired goal without creating a special needs trust, this paper concentrates on the creation of a special needs trust through the reformation of an existing trust agreement.

II. What is Reformation?

There are common law distinctions between the terms modification and reformation. Generally, a modification changes the agreement.¹ Reformation of an instrument, however, “correct[s] a mutual mistake made in preparing a written instrument, so that the instrument truly reflects the original agreement of the parties.”² The legal definition of reformation is “an equitable remedy by which a court will modify a written agreement to reflect the actual intent of the parties, usually to correct fraud or mutual mistake . . . the actual intended agreement must usually be established by clear and convincing evidence.”³ On the other hand, the legal definition of modification is simply, “a change to something; an alteration.”⁴

The common law distinction between reformation and modification is significant. Reformation of an instrument generally relates back to the time the instrument was originally executed, whereas a modification generally becomes effective at the time of its execution.⁵ To reform a written instrument, there must be sufficient proof of (1) an original agreement and (2) a mutual mistake in reducing the original agreement to writing.⁶ A modification generally becomes effective at the time of its execution, rather

¹ See, e.g., *Brinker v. Wobaco Trust Ltd.*, 610 S.W.2d 160, 166 (Tex. App.—Texarkana, 1980, writ ref’d n.r.e. April 1, 1981).

² *Cherokee Water Co. v. Forderhause*, 741 S.W.2d 377, 379 (Tex 1987) (citing *Brinker*, 610 S.W.2d at 163).

³ *Blacks Law Dictionary* 592 (2nd Pocket Ed. 2001)

⁴ *Id.* at 454.

⁵ Restatement (Third) of Property, § 12.1 cmt. f; see also, *Id.* at § 62, Reporter’s Note.

⁶ *Cherokee Water Co.*, 741 S.W.2d at 379.

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