INTRODUCTION TO SPECIAL NEEDS TRUSTS

A special needs trust is established for the benefit of an individual with disabilities. There are several types of special needs trusts, but the purpose of all special needs trusts is the same: to maximize resources and to administer trust assets without causing the beneficiary to lose eligibility for public benefits.

What Kinds of Public Benefits Are Protected with a Special Needs Trust?
Special needs trusts are intended to protect eligibility for means-tested (also called needs-based) benefits including Supplemental Security Income (SSI) and Medicaid. In Maine, the Medicaid program is known as MaineCare. An individual will only be eligible for these benefits if he or she has limited income and assets.

The existence of a special needs trust does not, by itself, make public benefits available. The beneficiary must already qualify for the public benefits program or qualify after the trust is established. If properly established, the transfer of assets to the trust and the existence of trust assets for the benefit of the beneficiary with disabilities will not cause a loss of benefits.

What Is a "Supplemental Needs" Trust?
Some lawyers prefer to use the term "supplemental needs" rather than "special needs." Occasionally the term "supplemental benefits" is also used. Some attorneys refer to first-party trusts as special needs trusts and to third-party trusts as supplemental needs trusts.

What Are the Differences Between First-Party and Third-Party Special Needs Trusts?

Third-Party Trusts. A third-party special needs trust is established by one person (a third party) for the benefit of the individual with disabilities. The person establishing the trust is referred to as the settlor (or grantor or trustor). This person is choosing to make some of his or her own assets available for the benefit of the individual with disabilities, possibly during the lifetime of the settlor or maybe upon the death of the settlor.

Parents and grandparents often establish third-party special needs trusts for their children or grandchildren who have disabilities that make them eligible for means-tested benefits. In some cases, the trusts come into existence upon the death of the settlor. In other cases, the trusts come into existence during the settlor's lifetime in a "freestanding" trust or living ("inter vivos") trust.

A testamentary third-party special needs trust may be included in the will of an individual whose spouse is in a nursing home or another long-term care setting. In those cases, the

trust for the surviving spouse comes into existence upon the settlor's death to hold and administer trust assets for the beneficiary. Note that a special needs trust one spouse creates for a surviving spouse cannot be created as an inter vivos trust. It must be created in the decedent's last will and testament.

There are relatively few rules governing third-party special needs trusts because the beneficiary never owned or controlled the assets that become part of the trust. Even so, it is important that the terms of a third-party special needs trust not create any entitlement on the part of the beneficiary to either income or principal from the trust. If the trustee has complete discretion whether to make distributions to the beneficiary, the trust principal and income will usually not be counted as available assets under the SSI or MaineCare rules.

While the principles involved in third-party special needs trusts are relatively simple, there are a myriad of choices involved in drafting the trust. In addition, the administration of a special needs trust can be tricky. A lawyer experienced with public benefits programs and special needs trusts should always be involved in the preparation of any third-party special needs trust.

First-Party Trusts. An individual with disabilities may own or receive assets that prevent eligibility or continued eligibility for means-tested public benefits. In these cases, it may be possible and advisable to transfer the individual's assets to a special needs trust to establish or re-establish eligibility for the means-tested public benefits. A first-party special needs trust (also called a self-settled trust, a d4A trust, an under-sixty-five trust, or a payback trust) is created with the assets of the individual with disabilities.

First-party special needs trusts are often established because an individual received a personal injury settlement (perhaps, but not necessarily, arising out of the incident that caused the disability) or an inheritance that was not directed to a third-party special needs trust. Sometimes individuals with pre-existing wealth determine that it would be advisable to create a special needs trust.

Federal law previously required that a first-party trust be established by a parent, grandparent, court-appointed guardian, or court. The Special Needs Trust Fairness Act passed in December of 2016 now allows for the individual with disabilities to establish his or her own first-party trust.

First-party special needs trusts may only accept the assets of a beneficiary who is under the age of 65. Also, most first-party special needs trusts must include a provision requiring repayment of state Medicaid agencies for any medical assistance that the beneficiary received during his or her lifetime, payable upon the death of the beneficiary, provided that such funds still exist in the trust. Such a provision is often called a "payback" provision.

In most cases, only first-party special needs trusts require a provision repaying the state for Medicaid benefits. Third-party special needs trusts (discussed above) do not ordinarily include a provision for repayment of government expenditures.

What Can a Special Needs Trust Provide for the Trust Beneficiary?

When the beneficiary of a special needs trust is receiving SSI benefits, the trustee must understand the effect on those benefits of paying for food or shelter from the trust or distributing cash to the beneficiary. The trust can provide many other goods and services including, for example, physical therapy, medical treatment, education, entertainment, travel, companionship, clothing, furniture and furnishings (such as a television or computer), and some utilities (like cable television or telephone service).

There are special rules regarding distributions made from special needs trusts (or from any third-party payor) for shelter. Those rules are difficult to navigate and depend heavily on the beneficiary's own situation. Because of this, the trustee should consult an attorney.

Is It Difficult to Act as Trustee of a Special Needs Trust?

The rules governing a trustee's actions can be complicated and confusing. The trustee must look to the language of the trust itself, be familiar with the law governing trusts generally, know how to properly file necessary tax returns, provide accountings as required, and also be aware of public benefits rules and the impact that the trust's distributions may have on the beneficiary's eligibility for benefits. Most trustees of special needs trusts will want to retain an attorney to provide them with continuing legal advice. Court accounting requirements and public benefit agency demands can significantly increase the level of complication.

While it is no substitute for competent and individualized legal advice, you can consult the Special Needs Alliance's Handbook for Trustees, available on the Special Needs Alliance's website at http://www.specialneedsalliance.org/free-trustee-handbook/.

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