



Printed in the Consumer Attorney's of San Diego's Trial Bar News, June/July 2001

Litigation Special Needs Trusts

by
Carol S. Battaglia

Copyright 2001

In 1990's, when many members of the Consumer Attorneys of California (then CTLA) noted the unfair result of plaintiffs winning awards only to lose their rights to Medi-Cal and other public benefits, the organization became instrumental in lobbying for legislative approval of special needs trusts.¹ Despite that success, special needs trusts remain an under-utilized settlement solution. If the ultimate goal of a personal injury award is to provide compensation for injury and disability and to improve the quality of the disabled person's life, added care must be used where clients are relying on public benefits. Unless carefully structured, a successful plaintiff on public benefits is often forced to spend virtually all of an award in order to be eligible for those continued benefits. When this happens, the compensation and benefit gained through the lawsuit has been lost for that plaintiff because, ultimately, the plaintiff can be in no better financial position than they were before the lawsuit. Even if a minor is not currently on public benefits, consideration must be given as to the likelihood that he or she will need public benefits upon reaching adulthood.

Generally speaking, there are two types of special needs trusts which preserve a beneficiary's public benefits. These are: 1) estate planning special needs trusts which allows parents or others to leave an inheritance to a disabled family member and 2) litigation special needs trusts, which are the focus of this article. The public benefits which are usually discussed with regards to litigation special needs trusts are SSI (Supplemental Security Income) and Medicaid (MediCal in California) and this article will be limited to those programs. Many states, such as California, automatically qualify a person for MediCal when they become eligible for SSI. These programs are "needs based" and intended for individuals who have no more than \$2,000 in countable assets such as checking and/or savings accounts, stocks, bonds, etc. Certain resources are considered "exempt" such as a residence of any value, a specially equipped motor vehicle and a properly created special needs trust.

Federal legislation for special needs trusts was passed on August 11, 1993² and the statutory authority can be found at 42 U.S.C.A. §1396p(d)(4)(A). This legislation carved out an exception in determining assets and income for Medicaid eligibility for certain trusts which contain:

“the assets of an individual under age 65 who is disabled and which is established for the benefit of such individual by a parent, grandparent, legal guardian or a court in

¹ On January 1, 1993, California became the first state in the country to pass legislation allowing for the management in trust of litigation proceeds for a disabled plaintiff [Probate Code §§3602(d), 3611(c)].

² Please see the Omnibus Budget Reconciliation Act of 1993 (OBRA'93)

the state will receive all amounts remaining in the trust upon the death of such individual up to an amount equal to the total medical assistance paid on behalf of the individual under a state plan . . .”

The definition of “disabled “ is the same as the one used for determining eligibility for SSI. The statute provides:

“An individual shall be considered to be disabled for purposes of this subchapter if he is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or which has lasted or can be expected to last for a continuous period of not less than twelve months (or, in the case of a child under the age of 18, if he suffers from any medically determinable physical or mental impairment of comparable severity.)³

In order to establish a special needs trust, California requires that the Court make the following specific findings: 1) that the minor or incompetent⁴ person has a disability that substantially impairs the person’s ability to provide for his or her own care or custody and constitutes a substantial handicap; 2) that the minor or incompetent person is likely to have special needs that will not be met without the trust; and 3) that the money to be paid to the trust does not exceed the amount that appears reasonably necessary to meet the special needs of the minor or incompetent person. [Probate Code §3604(b)]

In addition, the special needs trust must be drawn and approved by the court in connection with the approval of the minor’s, incompetent’s or disabled adult’s settlement. Certain drafting requirements must be included so that continued eligibility for public benefits is not jeopardized. There must be a provision requiring that all amounts remaining in the trust at the death of the beneficiary, up to the total amount that the state agency paid for the beneficiary’s medical expenses be repaid to the state. The trustee must be given absolute discretion to spend funds on behalf of the beneficiary. There can be no required disbursements nor can the beneficiary have direct access to the trust fund without jeopardizing SSI and MediCal eligibility. Furthermore, all liens must be satisfied before the creation of the special needs trust. The trust must be part of the overall settlement agreement and the proceeds must be paid directly to the trustee of the special needs trust. The proceeds are not protected by placement in the attorney’s trust account as that is considered constructive receipt; nor is it possible to create a special needs trust after a settlement agreement has been reached and the funds disbursed. Finally, periodic accountings need to be filed with the Probate Court.

³ 42 U.S.C.A. §1382c(a)(3)(A)

⁴ Although the Probate Code refers to minors or incompetents, references to an “incompetent person” are deemed to include “a person for whom a conservator may be appointed” [Probate Code §3603]. In most instances, a person who has satisfied the federal standard and is receiving SSI and Med-Cal is also a person “for whom a conservator may be appointed..” A conservator may be appointed for a person who voluntarily requests the appointment such as when a person is mentally competent but suffering from a physical impairment. [Probate Code 3603]

Once the special needs trust has been established, the trustee can be creative in finding ways that the trust can improve the quality of life for the beneficiary. In general, food, clothing and shelter (necessities) should not be provided by the trust because such expenditures would count against the SSI benefit and could reduce the benefit up to one-third of the payment. However, as long as the beneficiary receives even \$1 of SSI, he or she retains their Medi-Cal benefits. The trust can pay for any medical expenses which are not covered by Medi-Cal which can include alternative or experimental therapies. It can pay for a remodeling of a home, a specially equipped automobile of any value, including insurance, license fees and maintenance, additional attendant care and computer or other special equipment. The trust can also pay for dental care, non-generic drugs, physical and/or speech therapy, occupational therapy, psychotherapy and vocational rehabilitation.

A litigation special needs trust can provide a solution for those plaintiffs who need the greatest ongoing protection. It is also a cost-effective solution, because SSI benefits don't ever need to be repaid and Medi-Cal can only be reimbursed up to the amount remaining in trust, so if \$100,000 has been spent on medical care for the injured person, but only \$1,000 remains at the time of death, Medi-Cal can only recover \$1,000.