Changes for Special Needs Persons after July 1

1:00 p.m. - 1:30 p.m.

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MONDAY, JUNE 13
Special Needs Trusts in Iowa

Iowa State Bar Association
Annual Meeting
Elder Law Section Track

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And

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Before addressing the issue of special needs trust, this outline will provide a general overview of basic eligibility for medical assistance through the Medicaid program and will also provide a brief overview of planning alternatives.

I. FINANCIAL NEED – BASIC ELIGIBILITY STANDARDS

In order to plan for a person with disabilities it is critical that the program(s) under which the person is receiving benefits are confirmed as the eligibility standards vary. This outline will not go into any great detail in identifying the different programs, but will refer to some basic eligibility standards and a process to analyze planning alternatives.

A. Resource Eligibility

Some, but not all governmental programs base eligibility on financial need. Two examples of such programs are social security supplemental income (SSI) and Medicaid (Title XIX). Both utilize the methodology of the social security administration to determine countable resources and noncountable resources. Generally, a home, household goods, an automobile, health equipment, and prepaid burial accounts do not count. A special needs trust as defined by federal and Iowa statutory law is a noncountable resource. 42 USC 1396 p(d)(4)(A) and Iowa Code 633C.2.

Other assets, such as cash, investments, life insurance, and other hard assets, “count”. Under both SSI and XIX, a person may have only $2,000 in countable resources in order to satisfy resource eligibility.

B. Income eligibility

Both SSI and XIX, are financial needs based programs and have income eligibility limits, which are adjusted annually to reflect changes in the cost of living. If a person is eligible for SSI, he or she is eligible to receive XIX benefits. If his income is greater than the SSI limit, but less than the XIX limit, he may still be eligible for XIX benefits. In 2015, the SSI income limit is $733 per month, and the XIX limit is three times this figure, or $2199 per month.

Some programs, such as social security disability income (SSDI) and Medicare are NOT based on financial need, in which case the analysis of income and resources is not required.

The following planning worksheet may be used to help analyze the alternatives when financial need based programs are involved.
C. Planning worksheet

<table>
<thead>
<tr>
<th>Income</th>
<th>Resources</th>
<th>Noncountable Resources</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pension</td>
<td>Cash, investments etc</td>
<td>Home, household goods, health equipment, auto, and prepaid burial accounts</td>
</tr>
<tr>
<td>Social security</td>
<td></td>
<td></td>
</tr>
<tr>
<td>SSI Eligibility</td>
<td>$733</td>
<td>Special Needs trusts</td>
</tr>
<tr>
<td>XIX Eligibility</td>
<td>$2,199</td>
<td>Medicaid qualified annuity</td>
</tr>
</tbody>
</table>

II. TRANSFERS OF RESOURCES

A. TRANSFER OF RESOURCES

A question which often arises in the context of applying for benefits concerns transfers of resources.

The "Transfer of Resources" rules refer to transfers of resources for less than fair market value for the purpose of establishing eligibility for Medicaid. See Iowa Code 249A.3, subsections 7 and 11, and 441 Iowa Administrative Code 75.23.

In 2006, the Deficit Reduction Act (DRA), extended the lookback period for all transfers to 60 months.

A previous federal law, OBRA 1993, also required the states to enact "estate recovery" programs to recover assets from estate of decedents who transferred assets within the lookback periods and received state Medicaid benefits.

"Transfer of Resources" include, but are not limited to, establishing a trust, contributing to a charity, and removing a name from a resource. OBRA 1993 also enlarged this to include any action which reduces or eliminates an individual's ownership or control of property held with another. When a resource is transferred in exchange for compensation in the form of support or services, the value of the compensation must be compared to the value of the resource. Disclaimers are considered transfers of assets as well. Iowa Code 633E.15 (2015). 441 IAC 75.23(2) subsection 3.

B. PENALTIES FOR TRANSFERS

Under the 2006 Deficit Reduction Act (DRA) federal legislation, the beginning date for determining the period of ineligibility will change. For any transfers made after on February 8, 2006, the period of ineligibility begins on the date of the transfer, or the date when eligibility is applied for, whichever is later. This is a significant change as it could
mean that a person who seeks assistance due to health and financial need must be certain that he or she has not made any gifts or transfers in the five years before seeking assistance, or risk being found ineligible for benefits. Iowa essentially adopted these rules. See Iowa Code 249A.3 subsections 7 and 11, 441 IAC 75.23(1) et seq.

In addition to the penalty which is imposed upon the person applying for benefits, under Iowa law, the State may pursue the recipient of the transfer under certain circumstances. See Iowa Code 249F.

Any transfer for less than fair consideration while the transferor is receiving benefits, or within five years prior to the application, is presumed to be made for the purpose of obtaining governmental needs based benefits. There are some exceptions to this rule, such as transfers to a spouse, to a dependent or disabled child, or to a child who has lived with a parent which permitted the parent to stay at home rather than move to an institution. Iowa Code 249F.1 (2).

Such a transfer creates a “debt” which the State may pursue. At present, the State of Iowa utilizes the Department of Inspections and Appeals to investigate these matters and attempt collection or seek judgment in favor of the state against the transferors.

III. TRUSTS.

A. SPECIAL NEEDS TRUSTS

The special needs trust is a statutory creation. It was created by 1993 federal legislation, known as Omnibus Budget Reconciliation Act of 1993, commonly referred to as OBRA 1993. The special needs trust was one of three trusts specifically authorized by Congress which pertain to Medicaid eligibility. The citation for the federal legislation is 42 USC 1396p(d)(4)(A), which provides:

A trust containing the assets of an individual under age 65 who is disabled (as defined in section 1382c(a)(3) of this title) and which is established for the benefit of such individual by a parent, grandparent, legal guardian of the individual, or a court if 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 under this subchapter.

Subsequent to the OBRA 1993 legislation, the Social Security Administration adopted identical language for a Special Needs Trust. The Social Security operating manual elaborates slightly and provides:

“The statutory exceptions from the Medicaid trusts provision effective October 1, 1993, may affect the eligibility of certain SSI beneficiaries for Medicaid. Those exceptions are applicable to:
- Trusts established for the benefit of a disabled individual under age 65 containing assets of the individual by a parent, grandparent, legal guardian of the individual or a court, if the State will receive all amounts remaining in the trust upon the death of the individual up to an amount equal to the total medical assistance paid on behalf of the individual.”


Iowa has adopted the trusts created by Congress as part of OBRA 1993. The language for the Iowa special needs trust is found at Iowa Code Chapter 633C.1(7) “‘Medical assistance special needs trust’ means a trust or similar legal instrument or device that meets the criteria of 42 U.S.C. § 1396p(d)(4)(A) or (C).”

It must be noted that a statutory special needs trust is one that is self-settled. Trusts established by a fiduciary or a court on behalf of an incapacitated individual have routinely been treated by the DHS as self-settled.

Further regulatory authority exists under the Iowa Administrative Code at 441 IAC 75.24 which explains treatment of trusts established after August 10, 1993.

Stepping back from the Special Needs Trust for a moment to gain perspective, it is important to be aware of the general rules pertaining to trusts and how they affect eligibility for government benefits. Generally, if a person is applying for benefits and the person is entitled to income, or principal from the trust, the income and/or principal will be considered “countable” to the person. Depending upon the amount of his or her total income and resources, counting the trust income and resources may push her, or him over the eligibility limits.

If a person is the grantor of a revocable trust, the assets are counted for eligibility purposes. 441 IAC 75.24(2). For nonrevocable trusts, the amount distributed to the beneficiary will be considered available. 441 IAC 75.24(2)(b). In addition, if the trust was established within the five (5) year look back period, all of the corpus will be considered available. Iowa Code Section 249A.3(13). IAC 75.24(2).

As a result of these rules, persons often seek the establishment of a trust which will allow her, or him, to preserve the trust assets while also allowing her, or him to maintain eligibility for government benefits. The OBRA 1993 trusts mentioned above satisfy this goal. In addition, trusts established by third parties, or testamentary trusts (trusts established under a decedent’s will) are not required to be as narrowly drawn as the OBRA 1993 trusts. IAC 75.24(1)(b). Please remember that any distribution from any trust may be considered countable for income or resource purposes and that the trust should be drafted with this concern in mind.
II. 2015 amendment to Iowa Code Chapter 633C concerning special needs trusts.

The amendment significantly loosened the restrictions on the use of funds in a special needs trust.

Under the amendment “any income or assets added to or received by and any income or principal retained in a medical assistance special needs trust shall be used in accordance with a standard that is no more restrictive than specified under federal law. All distributions from a medical assistance special needs trust shall be for the sole benefit of the beneficiary to enhance the quality of life of the beneficiary, and the trustee shall have sole discretion regarding such disbursement to ensure compliance with beneficiary eligibility requirements. Any distinct disbursement in excess of one thousand dollars shall be subject to review by the district court sitting in probate.” 633C.2

This is significantly less restrictive than the old law which limited expenditures from a special needs trust to special needs of the individual which would not exist but for the medical needs of the individual and expressly stated that spending for basic needs was not permitted.

The amendment also makes it clear that the trust is required to submit an annual accounting to the district court. 633C.4

Because court approval was required for expenditures from a special needs trust under the old law, this does not appear to create any special burden on a trustee.

Michel Nelson of the Iowa Savings Bank prepared a side by side comparison of the language from 633C under the old law and the new law. A copy is attached as an appendix to this outline.

Medicaid eligibility and the administration of the Medicaid program is closely related to social security regulations for social security supplemental income (SSI). The social security administration has developed an operating manual for its various programs. It is referred to as the Program Operations Manual or POMS.

Because of the relationship between Medicaid and SSI, one could look to POMS for some guidance on the type and kind of expenditures that are likely to be approved by Medicaid as being for the “sole benefit” of the trust beneficiary.
Under POMS, a trust is established for the sole benefit of a disabled individual if it benefits no one else.\(^1\) Some third party payments are exempt from this sole benefit rule, including:

- Payments to a third party that result in the receipt of goods or services by the trust beneficiary;
- Payment of third party travel expenses which are necessary in order for the trust beneficiary to obtain medical treatment; and
- Payment of third party travel expenses to visit a trust beneficiary who resides in an institution, nursing home, or other long-term care facility (e.g., group homes and assisted living facilities) or other supported living arrangement in which a non-family member or entity is being paid to provide or oversee the individual’s living arrangement. The travel must be for the purpose of ensuring the safety and/or medical well-being of the individual.\(^2\)

In addition, reasonable compensation to a trustee for trust management and reasonable administrative costs are exempted from the sole benefit rule.\(^3\)

Allowable Administrative Expenses upon Death of Beneficiary: POMS provides some guidance on allowable post-death administrative expenditures, explicitly allowing only taxes due to the state or federal government because of the beneficiary’s death and reasonable fees for administration.\(^4\) POMS explicitly prohibits the payment of the following administrative expenditures prior to state reimbursement for medical assistance upon the death of the beneficiary:

- Taxes due from the estate of the beneficiary other than those arising from inclusion of the trust in the estate;
- Inheritance taxes due for residual beneficiaries;
- Payment of debts owed to third parties;
- Funeral expenses; and
- Payments to residual beneficiaries.\(^5\)

During the life of the beneficiary, administrative expenses are only allowed to be paid for by the SNT as permitted by the trust document.\(^6\)

Disbursements from the Trust:

The inquiry regarding proper disbursements from a trust centers on whether the disbursement would be considered income and would potentially impact SSI and Medicaid eligibility. The availability of SSI and Medicaid depends on an individual’s

\(^1\) POMS § 01120.201(F)(2)(a).
\(^2\) Id. § 01120.201(F)(2)(b).
\(^3\) Id. § 01120.201(F)(2)(c).
\(^4\) Id. § 01120.203(B)(3)(a), (c).
\(^5\) Id. § 01120.203(B)(3)(b).
\(^6\) Id. § 01120.203(B)(3)(c).
income, which is defined as “anything in cash or in kind which can be used for food or shelter.”

Thus, whether a disbursement is considered income to the beneficiary depends on the nature of the disbursement.

**Disbursements Considered Income:**

Cash paid directly to a beneficiary is unearned income to the beneficiary. If a beneficiary receives non-cash items from a third party as the result of a trust distribution, and the items *would not be* an excluded resource if retained a month after the receipt, this distribution *would be* in-kind income to the beneficiary. Disbursements resulting in food or shelter to the beneficiary are income.

**Disbursements Not Considered Income:**

Trust disbursements which are not in cash or are made to third parties not resulting in support and maintenance to the beneficiary are not income. Such disbursements may include:

- Educational Expenses
- Therapy
- Medical Services not covered by Medicaid
- Phone Bills
- Recreation
- Entertainment, etc.

In addition, if a beneficiary receives non-cash items from a third party as the result of a trust distribution, and the items *would be* an excluded resource if retained a month after the receipt, this distribution *would not be* income to the beneficiary.

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7 *Id.*. Payments for shelter can include payments for mortgages, real property taxes, rent, heating fuel, gas, electricity, water, sewer, garbage removal, and condominium expenses which may include any of those expenses. **ALI, Administering a Special Needs Trust: A Handbook for Trustees**, SR013 ALI-ABA 325 (2009).
8 POMS § SI 01120.201(I)(1).
9 *Id.* § SI 01120.201(I)(1)(a).
10 *Id.* (“For example, if a trust buys a car for the beneficiary and the beneficiary's spouse already has a car which is excluded for SSI, the second car is income in the month of receipt since it would not be an excluded resource in the following month.”).
11 *Id.* § SI 01120.201(I)(1)(b).
12 *Id.* § SI 01120.201(I)(1)(c).
13 *Id.*
14 *Id.* (“For example, a trust purchases a computer for the beneficiary. Since the computer would be excluded from resources as household goods in the following month, the computer is not income.”).
**Disbursements for Credit Card Bills:**

If a trust makes a disbursement to pay a credit card bill for food or shelter, this is in-kind support and maintenance and will be considered income the beneficiary.\(^{15}\) If the bill is for not for food or shelter, whether it is income depends on if the item paid for would be an excluded resource the following month.\(^{16}\)

**Disbursements for Gift Cards and Gift Certificates:**

Disbursements in the form of gift cards or gift certificates which can be used to purchase food or shelter, or can be sold for cash, are considered cash income to the beneficiary.\(^{17}\)

**Reimbursements to Third Parties:**

Reimbursements to third parties for funds paid for on behalf of the beneficiary are not income to the beneficiary unless the income and resources rules above apply (i.e., the reimbursement was for an item not excluded as a resource).\(^{18}\)

**I. Iowa’s Medicaid Requirements**

A state’s Medicaid manual may provide additional requirements for SNT compliance; however, Iowa is included in the majority of states in which the SSA makes its SSI-related Medicaid determinations, using the POMS requirements to do so.\(^{19}\)

While Iowa turns to the SSA in making these SSI-related Medicaid determinations and does not have its own Medicaid manual applicable to SNT requirements, the Iowa Medicaid Trust Program gives guidance on SNTs and their ability to expend funds for disabled individuals.\(^{20}\)

The Medicaid trust program provided the following list of key items that it looks for when evaluating a SNT.

1. The trust is established for the beneficiary by a parent, grandparent, legal guardian, or a court, or through a conservatorship or Power of Attorney.
2. The trust was established after August 10, 1993.
3. The trust is irrevocable, or the State’s interest is protected upon any modification or termination.
4. The beneficiary is under 65 years of age.

\(^{15}\) *Id.* § SI 01120.201(I)(1)(d).

\(^{16}\) *Id.* § SI 01120.201(I)(1)(d) ("For example, if the credit card bill includes restaurant charges, payment of those charges results in [in-kind support]. If the bill also includes purchase of clothing, payment for the clothing is not income.").

\(^{17}\) *Id.* § SI 01120.201(I)(1)(e).

\(^{18}\) *Id.* § SI 01120.201(I)(1)(f)

\(^{19}\) *Id.* § SI 01715.010(A)(3); see also Lewis, *supra* note 4, at 16.


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5. The beneficiary is disabled as determined by the Social Security Administration, Railroad Retirement Board, or the Disability Determination Services Bureau of the Iowa Department of Human Services.

6. The trust contains only the beneficiary’s assets and the initial source of the assets is identified either in the trust, in a schedule of assets, or in other information provided with the submission of the trust.

7. The State of Iowa is the residuary beneficiary of the trust, along with other states providing Medicaid.


9. The beneficiary is not the trustee and has no control over the trust.

10. Payment to the state at termination of the trust is for all Medical Assistance provided, not just the Medical Assistance provided during the term of the trust.

11. Pre-existing Medicaid liens, if any, pursuant to Iowa Code 249A.54 have been satisfied.

**Obtaining Department of Human Services Approval of Special Needs Trust**

As mentioned previously in the outline the SNT must be approved by the DHS. The process is administrative in nature. A copy of the trust should be provided to the case worker for the medical assistance beneficiary. The caseworker will review it with necessary personnel within DHS, including an internal referral to the Medicaid Trust Program. The DHS will provide notification when the trust has been approved.

Please note that this process must be followed even after a trust has been approved through a court proceeding in a guardianship or conservatorship matter, and even when the DHS has been a party to the proceeding. Likewise, even if a person has had direct contact with the Medicaid Trust Program, the trust must be provided to the DHS case worker and run through the DHS channels for approval.

**B. POOLED TRUSTS**

In addition to the special needs trust described above, OBRA also created a Pooled Trust. 42 U.S.C. p(d)(4)(C), Iowa Code § 633C.1(7). There is a key distinction between a Pooled Trust and a regular special needs trust. In a pooled trust, at the death of the life beneficiary, the funds in the beneficiary’s sub-account may be retained by the trust. If the funds are retained by the trust, the trust may use it for the benefit of other beneficiaries of this Pooled Trust, to provide benefits for indigent disabled persons, either by adding them as beneficiaries of the trust, or making a direct payment for such indigent person by paying for equipment, medication or other services.

Recently Iowa made a change in the way that it will handle administration of Special Needs and Pooled Trusts when it established the Medicaid Trust Program. This change should provide for better tracking of these trusts on behalf of the state as the Medicaid
Trust Program is supervised by Ben Chatman who also supervises the Estate Recovery Program in Iowa. Attached to this outline as an Appendix is a handout prepared by the Medicaid Trust Program which provides suggestions and guidelines about the operation of the three OBRA 1993 trusts under Iowa law.

C. MEDICAL ASSISTANCE INCOME ASSIGNMENT TRUSTS (Miller Trusts)

1. The income assignment trust (Miller trust) is used in those instances where the applicant’s income exceeds the monthly income eligibility amount. In 2016, this amount is $2199 per month. The Miller trust is a conduit which receives all of the applicant’s monthly income and allows only the qualifying amount ($2199 minus $1) to be disbursed to the applicant. The funds disbursed to the applicant are regulated as well. Ordinarily they are paid directly to the providers of medical assistance. In the event that the applicant has a healthy spouse (“community spouse”), a portion of the income is likely to be diverted to him or her.

2. It is also important to note that there is an upper limit on the income of the applicant in order to be eligible to use an income assignment trust. If his or her income is equal to or greater than 125% average cost of care in a residential facility in the State of Iowa, he will be over the limit. Iowa Code 633C, subparagraph 2. a. The fiscal year 7/1/16 to 6/31/17, this amount is $6,583.75. In some instances, if you demonstrate that the individual requires a higher level of care than regular residential care, the upper limit to use an income assignment trust will be adjusted upward. See Iowa Code 633C.3(3), a. through d.

3. As with the special needs trust described above, the State will receive all amounts remaining in the trust upon the death of the individual up to an amount equal to the total medical assistance paid on behalf of the individual.

D. Discretionary Support Trust:

The Iowa Court of Appeals has ruled that the provisions of a testamentary trust which included discretion in the trustee to pay for the care, support, maintenance, and education of a disabled beneficiary was a support trust which could be reached in satisfaction of an enforceable claim for necessary services rendered to the beneficiary. Strojek v. Hardin County (Iowa Court of Appeals 1999) 602 NW 2d 566, 568.

The Strojek case returned to the Iowa Court of Appeals in February of 2002 to determine if payments for “vocational services” were within the discretion of the trustee as part of the beneficiary’s basic needs. The Court of Appeals concluded that the trust was broader than “basic needs” as it directed the trustee, in its discretion, to provide for “proper care, support, maintenance and education.” The court concluded that vocational, residential and maintenance were part of proper care, support, maintenance and education of the
beneficiary. As a result, the reasonable cost for vocational services, (in this instance $34 per day for 200 days per year) were to be included as part of the beneficiary’s basic care and counted for purposes of determining eligibility. Strojek v. Hardin County (Not reported in NW 2d, 2002 WL 180377 (Iowa App 2002)).

In the 2004 legislative session, the Iowa Trust Code was amended to specifically address this issue and state that in the construction of trust language that the language of the trust which is discretionary should prevail over any other interpretation of the language. Iowa Code Section 633A.4702.

In December of 2004, the Iowa Supreme Court handed down a decision in the case of In the Matter of George G. Barkema (690 N.W.2d 50). This case also involved a discretionary support trust. The issue was whether the State of Iowa, under the estate recovery statute had a right to seek recovery from the trust for benefits paid by the trust, following the death of the life beneficiary of the trust. The court found, that under the language of the trust in question, Lois, the life beneficiary had the right to expect at least a minimum level of support, within the reasonable discretion of the trustee. Since she could expect, or had a right to expect such support, the Iowa Supreme Court found that her creditors could expect similar support and under the terms of this trust had the right to pursue recovery.

In March of 2009, the Iowa Supreme Court further elaborated on discretionary trusts in the Matter of the Estate of Eleanor Gist, 763 N.W.2d 561. In the Gist case, the court examined the terms of a trust to determine whether the trust would be available pursuant to the decision entered in Barkema above. The court, after careful examination of the trust, determined that it was a "discretionary" trust with the standards, and to the extent that the standards were enforceable, there was an interest in trust which was subject to the estate recovery.

An Iowa Court of Appeals decision in the case of Kinsel (February 10, 2010), 2010 WL 446551 confirmed the rule of Barkema and Gist that the beneficiary of a discretionary trust had an “interest in trust” subject to an estate recovery claim under Iowa Code Section 249A.5.

Also it is worthy of note that there was a case in the 10th Circuit concerning special needs trusts and whether or not the special needs trust might be treated as a resource in determining eligibility. In that case, there was a special needs trust which appeared to be properly drafted but the problem occurred with the administration of the trust. As it turned out, the trust was administered in a fashion that allowed expenditures and made expenditures for routine things such as home furnishings, home maintenance and life insurance on a parent of the beneficiary. Since these were not special needs, it was determined that the trust had not been administered "for the sole benefit" of the disabled individual and therefore would be considered a countable resources for purposes of eligibility. Hobbs v. Zenderman, 579 F3d 1171 (10th Cir 2009) . The Hobbs case points out how important it is not only for the trust to be properly drafted but properly administered.
E. Iowa Code Chapter 634A Supplemental Needs Trust:

This chapter of the Iowa Code allows for the establishment of a trust for a disabled person to provide for the person’s supplemental needs. It is intended as a discretionary trust. It allows for payments for basic living expenses such as food, shelter and clothing, with the proviso that such expenditures shall only be used to supplement government benefit programs. 634A.2. A trustee must be very careful in administering such a trust. If distributions are made for basic needs, the DHS will consider the assets as available, which could result in an individual being over resources or income and losing governmental benefits.