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THE WRONGHEADEDNESS OF THE POMS POOLED TRUST RULES AND AN UNFORTUNATE BUT RECENTLY NOTED CHINESE PARALLEL

THOMAS E. SIMMONS*

Supplemental needs trusts of the pooled trust variety have offered important dignity-enhancing protections for individuals with disabilities for several decades. A pooled trust, properly structured according to Congressional requirements, allows the wealth of an individual with disabilities to be overseen by an independent third party trustee, supplementing without displacing means-tested government programs like Medicaid and Supplemental Security Income. Beginning in 2012, the Social Security Administration imposed new burdensome requirements on pooled trusts through its informal POMS manual. Those new requirements have intentionally or unintentionally eliminated as a practical matter the availability of pooled trusts in many states. This unfortunate result can be paralleled with recent observations about the shortcomings of supplemental needs trust legislation and regulations in the People's Republic of China.

Stephen Tensmeyer's insightful note, *Modernizing Chinese Trust Law*, examines and critiques Chinese trust laws.¹ In the marrow of his article, he identifies the chief problem with China's trust laws. By collapsing any distinction between large-scale commercial trust ventures (like those targeted by antitrust legislation) and private trusts (like those studied in any law school Trusts and Estates course),

* Assistant Professor, University of South Dakota School of Law.

¹ Stephen Tensmeyer, Note, *Modernizing Chinese Trust Law*, 90 N.Y.U. L. REV. 710 (2015).

the aim of protecting wealth for a loved one by means of a trust structure was made, perhaps unintentionally, unobtainable.²

Currently, business trusts are in widespread use in China.³ Private trusts are essentially unknown.⁴ A particularly rich section of Tensmeyer's analysis considers the barriers to implementing self-settled pooled trusts for individual beneficiaries with disabilities in China.⁵ He identifies the largest obstacle to pooled trusts as the trustee qualification requirements. Coincidentally—and tragically—due to an informal interpretive shift by the Social Security Administration in 2012, the same obstacles now unfairly interfere with the use of pooled trusts for individuals with disabilities in the United States.⁶

As Tensmeyer explains, a trust which pools investments—while maintaining separate accounts for each beneficiary—can supplement government benefits for individuals with disabilities.⁷ Properly structured, eligibility for government benefits can be retained. Because of the economies of scale realized by pooling accounts, even relatively small account balances can be managed efficiently. Pooled trusts offer enormous benefits to individuals with disabilities.

² *Id.* at 734-40.

³ See also John H. Langbein, *The Secret Life of the Trust: The Trust as an Instrument of Commerce*, 107 YALE L.J. 165, 166 (1997) (arguing that “the American legal intellectual tradition, which characterizes the trust as a branch of the law of gratuitous transfers, is at odds with the reality of American trust practice” because “[i]n truth, most of the wealth that is held in trust in the United States is placed there incident to business deals, and not in connection with gratuitous transfers.”). Compare Kai Lyu, Article, *Re-Clarifying China's Trust Law: Characteristics and New Conceptual Basis*, 36 LOY. L.A. INT'L & COMP. L. REV. 447, 449 (2015) (noting that in China, “three demands had fueled the rapid growth of trust: (1) banks setting up trust subsidiaries to provide financial services that banks were not allowed to do; (2) local governments establishing trust investment companies to channel extra-budgetary funds to local infrastructure projects for higher returns; and (3) the central government creating trust companies to bridge overseas capital with cash-starved domestic enterprises.”); The Chinese Trust law was enacted in 2001. Tensmeyer, *supra* note 1, at 717.

⁴ Adam G. Province, *Killing Me Softly: A Comparative Review of Chinese Inheritance Law to Address the Problem of Elder Abuse and Neglect in the United States*, 22 IND. INT'L & COMP. L. REV. 71, 90 (2012) [hereinafter, PRC Trust Law]; See also Tensmeyer, *supra* note 1, at 721 (observing that “the trust industry may be the second largest industry in China's financial services sector” but “[f]unctionally, they are like any other investment vehicle” rather than private trusts).

⁵ Tensmeyer, *supra* note 1, at 734-40.

⁶ On pooled trusts generally, see CLIFTON B. KRUSE, JR., THIRD-PARTY AND SELF-CREATED TRUSTS: PLANNING FOR THE ELDERLY AND DISABLED 11-12 (2nd ed. 1998); RENÉE C. LOVELACE, POOLED TRUST OPTIONS: A GUIDEBOOK (2010). See also *infra* note 14.

⁷ Tensmeyer, *supra* note 1, at 735 (citing Abraham J. Perlstein, *Comprehensive Future Care Planning for Disabled Beneficiaries*, EST. PLAN. 360, 365-66 (Oct. 2000)).

Under China's 2001 Trust Law, only an entity with legal personhood may exercise the powers of a trustee.⁸ The charitable Chinese associations benefitting individuals with disabilities which Tensmeyer classifies as "semi-official" seem to lack explicit legal personhood.⁹ Moreover, it appears that only "trust companies" (that is, financial institutions which are engaged in trust business and following specific regulatory requirements) can serve as trustees of Chinese trusts, whether commercial or private.¹⁰ Thus, the availability of pooled trusts for Chinese citizens with disabilities has been (with no pun intended) crippled.

On this side of the Pacific, pooled trusts for individuals with disabilities developed even before official Congressional recognition with the Omnibus Budget Reconciliation Act of 1993 ("OBRA '93") and the Foster Care Independence Act in 1999.¹¹ Pooled trusts are often referred to as "(d)(4)(C)" trusts on account of the particular subsection in federal law which describes and authorizes them.¹² Pooled trusts can be contrasted with other similar trusts like (d)(4)(A) trusts.¹³ Among the requirements for establishing a pooled trust account so as not to disqualify the beneficiary from Medicaid or Supplemental Security Income benefits, Congress mandated that the trust be "established and managed by a non-profit association." More specifically, the straightforward statutory characteristics of a pooled trust are that the trust contain the assets of an individual with disabilities and meet four prerequisites:

- (i) The trust is established and managed by a nonprofit association.

⁸ PRC Trust Law, *supra* note 4, art. 24.

⁹ See Tensmeyer, *supra* note 1, at 737. These charitable Chinese associations do "not seem to have legal personhood." *Id.*

¹⁰ See *id.* at 727-28 (noting that if regulatory restrictions in China seemingly drafted for application to large-scale commercial trust ventures "apply to family and public interests trusts, those small-scale trust forms will be virtually impossible.").

¹¹ Omnibus Budget Reconciliation Act (OBRA '93) of 1993, Pub.L. No. 103-66 (codified as amendments to 42 U.S.C. § 1396 *et seq.*) (containing significant revisions to the Federal Medical Assistance (or Medicaid) program); Foster Care Independent Act of 1999, Pub.L. No. 106-169 (codified at 42 U.S.C. § 677) (amending Part E of Title IV of the Social Security Act). For the pre-OBRA '93 history of pooled trusts see Kathleen Kientz, *Pooled Disability Trusts: A History and Survey of their Use in the United States*, 17 NAELA NEWS 20 (December 2005/January 2006), http://www.elderlawmaine.com/articles/NAELA_pooled.pdf.

¹² 42 U.S.C. § 1396p (d)(4)(C) (2012).

¹³ 42 U.S.C. § 1396p (d)(4)(A) (2012).

(ii) A separate account is maintained for each beneficiary of the trust, but, for purposes of investment and management of funds, the trust pools these accounts.

(iii) Accounts in the trust are established solely for the benefit of individuals who are disabled (as defined in section 1382c(a)(3) of this title) by the parent, grandparent, or legal guardian of such individuals, by such individuals, or by a court.

(iv) To the extent that amounts remaining in the beneficiary's account upon the death of the beneficiary are not retained by the trust, the trust pays to the State from such remaining amounts in the account an amount equal to the total amount of medical assistance paid on behalf of the beneficiary under the State plan under this subchapter.¹⁴

When an individual with a disability qualifies for Medicaid or Social Security Income (SSI) benefits but for their excess wealth, transferring or giving property away is seldom an option on account of divestment penalties which will render the individual ineligible.¹⁵ These divestment penalties function to discourage gifts. While transfers to a spouse escape the divestment penalties, the resources and assets of a spouse are also considered in the context of Medicaid and SSI eligibility.¹⁶ Transfers to a child with a disability and certain other transferees are also exempt from the reach of divestment penalties but are only available in limited circumstances.¹⁷ As a result, in most circumstances, an individual with more than \$2,000 in countable resources can neither qualify for Medicaid or SSI and cannot accelerate their eligibility by divesting themselves of assets.¹⁸ Only two options are typically available: spending down wealth until impoverishment is achieved or transfer assets to the trustee of an irrevocable (d)(4)(A) trust or (d)(4)(C) trust.

Moreover, only the former option (spending down to defined levels of impoverishment) is available if the individual with a disability is age 65 or older. Transfers to a (d)(4)(A) trust are only

¹⁴ 42 U.S.C. § 1396p (d)(4)(C) (2012).

¹⁵ 42 U.S.C. § 1396p (c) (2012).

¹⁶ 42 U.S.C. § 1396p (c)(2)(A)(i)(2012).

¹⁷ See 42 U.S.C. § 1396p (c)(2)(A)(ii) (2012) (describing exempt transfers to a disabled child); 42 U.S.C. § 1396p(c)(2)(A)(iii) (2012) (describing exempt transfers to “a sibling of such individual who has an equity interest in such home and who was residing in such individual’s home for a period of at least one year”).

¹⁸ 42 U.S.C. § 1396a (m)(1)(c) (2012); 42 U.S.C. § 1382b (2012).

permitted for individuals under age 65 on account of the governing statute.¹⁹ Sometimes (d)(4)(A) trusts are referred to by their nickname, “under-65” trusts. Transfers to a (d)(4)(C) trust—while seemingly permissible under the statutory text—have been determined to fall within the divestment penalty rubric by several courts.²⁰ A good part of the challenges for disabled individuals with limited resources (or their attorney, if they can afford one or locate a *pro bono* advocate) is navigating these complex eligibility rules which are governed by indefensibly poor statutory draftsmanship, despite the relative clarity of the core requirements of a pooled trust. One court has called the Medicaid/SSI eligibility statutes some of “the most completely impenetrable texts within human experience.”²¹

For many individuals with disabilities, a non-pooled trust is infeasible because an experienced and reputable trustee (typically a corporate trustee with a background in the unique challenges of administering supplemental needs trusts) cannot be located. Individual trustees (e.g., family members) are rarely suited to the task.²² Corporate trustees are more objective and trustworthy, but minimum trustee fees may be too high for the modest size of the assets and corporate trustees are often unwilling to accept the office of trustee when a modest trust *res* is involved.²³ The attorney fees incurred in drafting a non-pooled trust may also be a deterrent. With pooled trusts, drafting costs are eliminated because a master trust agreement is typically employed and ongoing costs are also competitive with (d)(4)(A) trust administration costs.²⁴

¹⁹ See 42 U.S.C. § 1396p (d)(4)(A) (2012) (describing a (d)(4)(A) trust as one containing “the assets of an individual under age 65”).

²⁰ *Ctr. for Special Needs Trust Admin., Inc. v. Olson*, 676 F.3d 688, 703 (8th Cir. 2012); *In re Pooled Advocate Trust*, 813 N.W.2d 130, 146-47 (S.D. 2012).

²¹ *Rehab. Ass’n of Va., Inc. v. Kozlowski*, 42 F.3d 1444, 1450 (4th Cir. 1994).

²² See BARBARA D. JACKINS, RICHARD S. BLANK, KEN W. SHULMAN & HARRIET H. ONELLO, *MANAGING A SPECIAL NEEDS TRUST: A GUIDE FOR TRUSTEES* 88 (2012) (noting problems with the use of independent trustees of supplemental needs trusts including an “implied restriction” by the Social Security Administration that parents may not act as trustees for disabled child-beneficiaries).

²³ LOVELACE, *supra* note 6, at 7. “[S]ome individuals and families will be more inclined to commit to a plan when there is a pooled trust available.” *Id.*

²⁴ See Jacqueline D. Farienella, Note, *Come on in, the Water’s Fine: Opening up the Special Needs Pooled Trust to the Eligible Elderly Population*, 14 ELDER L.J. 127, 157 (2006) (describing the fee structure of an Illinois pooled trust).

Pooled trusts offer two other advantages over (d)(4)(A) trusts. First, when a beneficiary passes away, a Medicaid agency “payback” requirement can be avoided to the extent that the beneficiary’s sub-account funds are retained for the benefit of other individuals with disabilities served by the nonprofit manager of the trust.²⁵ Second, the individual herself may establish a pooled trust, but may not establish her own (d)(4)(A) trust; it must instead be established by a parent, grandparent, or guardian.²⁶ Thus, there are several important advantages to pooled trusts. But both (d)(4)(A) and pooled trusts fulfill a function, the importance of which is difficult to understate, meaningfully improving the quality of life for individuals with disabilities yet retaining eligibility for both Medicaid and Social Security benefits.²⁷

The Social Security Administration utilizes a Program Operations Manual System (“POMS”) as internal policy and guidance to its field workers.²⁸ Although POMS does not have the force of law, it is considered persuasive authority.²⁹ In 2012, the Social Security Administration adopted a new POMS provision.³⁰ That provision required nonprofit organizations to “maintain ultimate managerial control” over pooled trusts and be responsible for “determining the amount of the trust corpus to

²⁵ See *supra* text accompanying note 14.

²⁶ Compare 42 U.S.C. § 1396p(d)(4)(A) (2012) with 42 U.S.C. § 1396p(d)(4)(C)(iii) (2012); See also *Draper v. Colvin*, 779 F.3d 556, 563 (8th Cir. 2015) (affirming the invalidity of a (d)(4)(A) trust created by the beneficiary’s parents acting as her agents under powers of attorney rather than in their individual capacities). The Special Needs Trust Fairness Act of 2015 would change this result by adding the words “the individual” to the list of persons who may establish a (d)(4)(A) trust. See also H.R. 670 114th Cong. (as passed by Senate, Sep. 9, 2015).

²⁷ Renée Lovelace, *The Dark Side of Pooled Trusts*, 14 NAELA Q. 6, 7 (Summer 2001).

²⁸ See generally, Taryn D. Walker, *Comment, Congress or the Social Security Administration: Who Defines a Special Needs Trust?*, 48 WAKE FOREST L. REV. 1055, 1057 (2013) (noting that “POMS provides interpretive rules within the SSA; therefore, the agency may supplement or amend the POMS at any time without opportunity for public notice and comment.”); See also Melissa Reiner Greener, Note, *The Social Security Administration’s Representative Payee Program: An Act of Benevolence or Cruelty?*, 12 CARDOZO L. REV. 2025, 2033 n. 43 (1991) (emphasizing that “the POMS is only a compilation of internal instructions for SSA employees to follow in performing their duties under the statute and regulations [and] is not ‘the law’ in any sense of the word -- it is not considered binding on administrative law judges, the SSA Appeals Council, or federal courts.”) (citing *Briggs v. Sullivan*, 886 F.2d 1132, 1144 (9th Cir.1989)).

²⁹ Cf. *Schweiker v. Hansen*, 450 U.S. 785, 789 (1981) (per curiam) (concluding that “the Claims Manual is not a regulation” and “has no legal force” insofar as binding the Social Security Administration).

³⁰ POMS § SI 01120.225 (2012).

invest” as well as “making the day-to-day decisions regarding the health and well-being of the pooled trust beneficiaries.”³¹ The Social Security Administration’s manual explains:

If a non-profit association employs the services of a for-profit entity, the non-profit association must maintain ultimate managerial control over the trust. The for-profit entity may handle certain trust functions on behalf of the non-profit association; however, the use of a for-profit entity must always be subordinate to the non-profit managers of a pooled trust under section 1917(d)(4)(C).

For example, the non-profit association must be responsible for:

- determining the amount of the trust corpus to invest;
- removing or replacing the trustee; and
- making the day-to-day decisions regarding the health and well-being of the pooled trust beneficiaries.

NOTE: This list is not intended to be exhaustive. These are a few examples of the type of authority that must vest in the non-profit association.³²

Although the new POMS provision did not expressly require nonprofits to serve as trustees of pooled trusts (which would clearly exceed the Congressional text), it did require nonprofits to exercise the fundamental powers of a trustee: those of investments and distributions.³³ As a practical matter, then, the POMS now require nonprofit entities to exercise the traditional powers of a trustee.

Here, sadly, the POMS intersected with state banking and trust company laws. Although these laws vary, states typically allow entities and institutions to serve as trustees and exercise trustee powers only if authorized under similar rubrics to which financial institutions offering trustee services must adhere. State laws may provide exceptions for trustees serving without compensation or for charities serving as trustees of trusts of which the charity is also a beneficiary.³⁴ New York, for example, accords

³¹ POMS § SI 01120.225(D) (2012).

³² *Id.*

³³ See UNIF. TRUST CODE § 803 (2000).

³⁴ *E.g.*, OHIO REV. CODE ANN. § 1111.01(G)(3) (1999) (excluding any “charity, an officer or employee of a charity, or a person affiliated with a charity, serving as trustee of a charitable trust of which the charity, or another charity with a similar purpose, is a beneficiary” from fiduciary oversight requirements); S.D. CODIFIED LAWS § 51A-6A-1(7) (2015) (defining a “fiduciary for hire” subject to Division of Banking oversight as “acting as an administrator, conservator, custodian, executor, guardian, personal representative, or trustee, for any person, trust, or estate for compensation or gain or in anticipation of compensation or gain”); *See also* 19 ILL. PRAC., ESTATE PLANNING & ADMIN. § 216:8 (4th ed. 2015) (noting that under Illinois law: “A corporation must comply with the provisions of the Trust Company Act to be qualified to act as trustee.”).

with this approach.³⁵ Unless an exception applies, state law often bans both for-profit and nonprofit entities from acting as a trustee absent compliance with appropriately onerous requirements such as capital reserves, audits, and other mandates.³⁶ These requirements are simply beyond the capacity of most nonprofit organizations.

Prior to the 2012 POMS, nonprofit organizations could qualify as having “established and managed” a pooled trust (as Congress required) by first creating the master trust agreement and thereafter ruling on applications to join the trust while exercising oversight and supervision of an institutional trustee.³⁷ This approach permitted nonprofit organizations to make a pooled trust account available to individuals with disabilities while engaging the expertise and resources of an institutional trustee to perform investment and distribution functions. The 2012 POMS eliminated the availability of that kind of pooled trust structure by requiring nonprofit organizations to exercise trustee powers, powers that were unavailable to those nonprofits on account of state banking laws and regulations.³⁸

The problems which prohibit the use of the pooled trust structure in China—unnecessary barriers to qualifying as a trustee—parallel the same problems introduced by the Social Security Administration’s changes to its POMS.³⁹ State banking laws or regulations which require close oversight over institutional trustees are not misplaced, but the POMS is. Congress clearly stopped

³⁵ *E.g.*, *Matter of Nichols*, 475 N.Y.S.2d 787, 787 (Sur. Ct. 1984) (denying a church’s request to serve as an executor); *See also, e.g.*, *Yandell v. Wilson*, 183 So. 382, 385 (Miss. 1938) (holding that where a trust settlor delivers assets to a bank to hold as trustee and the bank is not qualified to act as a trustee, the settlor, as president of the same bank, is deemed to hold the assets as trustee in a personal capacity).

³⁶ *See* GEORGE GLEASON BOGERT, GEORGE TAYLOR BOGERT, & AMY MORRIS HESS, *BOGERT’S TRUSTS AND TRUSTEES* § 131 n.5 (2015) (citing corporate trustee qualification statutes and case law from several jurisdictions)

³⁷ *See, e.g.*, *Pooled Advocate Trust*, 813 N.W.2d at 133-34 (describing a (d)(4)(C) trust wherein “Pooled Advocate Trust, Inc. (PATI)” was a “managing corporation for a Medicaid pooled trust” while “Great Western Bank of Rapid City, South Dakota is the trustee.”). In the interests of disclosure, the author of this essay previously served as President of PATI and represented PATI in the aforesaid case. PATI has since dissolved on account of the 2012 POMS impediments described herein.

³⁸ *See supra* notes 17-18.

³⁹ *Tensmeyer, supra* note 1, at 737-38 (concluding that under Chinese law “[a]n entity seeking to manage a noncommercial collective trust would likely” have to qualify as a “trust company”).

short of requiring nonprofits to serve as trustees of pooled trusts; rather, nonprofits must be involved with the creation and administration of the trusts; to establish and manage. The 2012 POMS merely pay lip service to this nuance, noting in one breath that “the non-profit manager(s) may employ the services of a for-profit entity to manage some of the financial activities of the trust” yet mandating that the nonprofit exercise “ultimate managerial control over the trust” and be responsible for investment decisions as well as distribution decisions.⁴⁰ By this stroke, the Social Security Administration in effect required nonprofits to act as trustees.⁴¹

Tensmeyer’s proposed solution to China’s trustee qualifications dilemma is reform to the Chinese regulations.⁴² Reform or revisions to POMS seems unlikely, but courts have set aside POMS provisions which exceed the statutory framework.⁴³ By requiring nonprofits to retain ultimate managerial control over the primary functions of a trustee, the POMS *de facto* require that nonprofits act as trustees. Not only does this present serious practical difficulties for many nonprofit organizations, and in fact eliminates as a practical matter the availability of pooled trusts in many states, it exceeds the congressional text describing the requirements of pooled trusts. POMS provisions—exempt from the notice and comment requirements of regulations—should only be given judicial deference to the extent they have the power to persuade.⁴⁴ The 2012 POMS amendments relative to pooled trust trustee requirements are unpersuasive as well as contrary to the relevant Congressional text. They should be repealed by the United States Social Security Administration or jettisoned by the

⁴⁰ POMS § SI 01120.225(C)-(D) (2012).

⁴¹ See *Ramsdell v. Union Trust Co.*, 519 A.2d 1185, 1192 n.9 (Conn. 1987) (noting that a trustee’s duty to distribute is a non-delegable duty).

⁴² Tensmeyer, *supra* note 1, at 740-41.

⁴³ *E.g.*, *Oteze Fowlkes v. Adamec*, 432 F.3d 90 (2d Cir. 2005) (assuming that even if POMS “should be afforded deference generally” that the court “need not afford any deference to the manuals here, because the plain language of the statute and its implementing regulation do not permit the construction contained within the manuals”) (internal citation omitted); *See also* *Tejada v. Apfel*, 167 F.3d 770, 775 (2d Cir. 2009) (emphasizing that “ordinarily, where the POMS are inconsistent with the statute, we will not apply them”) (citation omitted).

⁴⁴ *Lockwood v. Commissioner*, 616 F.3d 1068, 1073 (9th Cir. 2010) (citations omitted).

courts. China, likewise, should modify its statutes or regulations and make available pooled trusts for individuals with disabilities.