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Pooled Trusts

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Pooled Trusts

by Thomas E. Simmons*

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In March, April, and June of this year, three important court decisions resulted in a negative impact for pooled trusts serving older individuals with disabilities throughout the country. The first case, In re Pooled Advocate Trust, Inc., was decided by the South Dakota Supreme Court.[i] The second case, Center for Special Needs Trust Administration, Inc. v. Olson, was decided by the Eight Circuit Court of Appeals, originating out of North Dakota.[ii] The third case, Lewis v. Alexander, decided by the Third Circuit Court of Appeals, originated out of Pennsylvania.[iii] All three courts concluded that Medicaid ineligibility penalties could be assessed against disabled individuals funding a pooled trust if the individual was age 65 or older at the time of funding the trust.

Pooled trusts are creatures of state and federal law, and the specific requirements for establishing a pooled trust are set forth in state administrative rules and federal Medicaid statutes. Medicaid was enacted by Congress and signed by President Lyndon Johnson as part of Title XIX of the Social Security Act.[iv] Medicaid is a cooperative federal-state program designed to provide medical treatment and long-term care services for needy persons. States electing to participate in the Medicaid program must develop Medicaid plans consistent with the federal Medicaid statute, regulations, and administrative rules.[v] As a condition of receipt of federal Medicaid funds, a state plan must comply with federal laws and regulations.[vi]

Medicaid is thus a creature of federal law, administered on a state-by-state basis. Because Medicaid is a needs-based program, eligibility is governed, in part, by whether the individual is sufficiently financially impoverished.[vii] Eligibility is "means tested" and applicants must satisfy both resource and income limitation rules before eligibility is granted in South Dakota by the South Dakota Department of Social Services ("DSS"). A single person receives long-term care Medicaid eligibility when his or her countable resources do not exceed $2,000 in value and his or her income is less than stated maximum monthly amounts.[viii] There are other eligibility requirements as well, such as residency.[ix]

States that voluntarily elect to participate in the Medicaid program (and all 50 States do, including south Dakota[x]) must comply with the eligibility requirements set by Congress. Accordingly, in South Dakota, DSS must comply with Congress' eligibility requirements. In the In re Pooled Trust appeal, DSS suggested that as the rule-maker, it has unfettered discretion to determine when eligibility for Medicaid applicants should be granted and when it should be denied -- even to the extent of ignoring all of the trust rules entirely. Eligibility requirements established by states which elect to participate in the Medicaid program may be more liberal than those set by Congress, but not more restrictive.[xi] Any attempts by states or Medicaid Agencies to be more restrictive are preempted by federal law.[xii]

The long-term care Medicaid rules consider an individual's gifts or "divestments" for less than fair market value and how such transfers impact eligibility for the program.[xiii] The divestment rules constrain the practice of becoming impoverished by aggressively conveying valuable assets to one's heirs, then applying for Medicaid benefits. Divestments occurring within a 60-month "look-back" period result in a "transfer penalty,"[xiv] meaning a period of Medicaid ineligibility; the larger the gift, the longer the penalty period.[xv]

The "Medicaid Divestment Penalty Divisor" is the number used to calculate the length of a Medicaid ineligibility period when a gift occurred within the 60 months prior to the date of a Medicaid application. In 2012, this number is $5,204. For every $5,204 in gifts, a penalty period of one month is imposed. For example, if a Medicaid applicant made gifts totaling $20,800 to her five adult children three years before applying for Medicaid, a four-month period of Medicaid ineligibility would be imposed, running from the date the individual would have otherwise been Medicaid eligible.

Trusts are also discussed in the Medicaid rules.[xvi] The Medicaid program generally deems trust assets to be resources fully available to the beneficiary where the grantor has retained any beneficial rights over funds conveyed to a trust. When an irrevocable trust "contains any provisions under which payment from the trust may be made to or for the benefit of the individual, the entire portion of the principal or income on the principal from which payment to the individual could be made is considered a resource."[xvii] There are no transfer penalties for conveying assets to a trust for one's own benefit, but there are penalties for conveying assets to a trust for a third party's benefit unless the transfer falls within narrow exceptions discussed below (*e.g.*, for transfers to a trust for a disabled child).

Thus, the general rule is that where the grantor has retained beneficial rights, the trust assets are considered resources available to the beneficiary to the fullest possible extent that the Trustee's discretion could be exercised. But, there are three limited exceptions. For three specific types of trusts, the deemed resource availability rules of self-settled trusts are suspended. The three types of trusts are "(d)(4)(A)" trusts, "(d)(4)(B)" trusts and "(d)(4)(C)" trusts.[xviii] These trusts were first recognized by the Omnibus Budget Reconciliation Act of 1993 (commonly known as OBRA '93).[xix]

A "(d)(4)(A)" trust is only available to individuals under the age of sixty-five (65) who are disabled.[xx] These are commonly referred to as "payback" or "under 65" trusts. To qualify as a (d)(4)(A) trust, the State Medicaid Agency must 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. This is commonly known as a "payback" requirement. A payback trust can only be funded by individuals with disabilities age 64 or younger.

A "(d)(4)(B)" trust may be composed of only pension, Social Security, and other income to the individual.[xxi] These trusts are referred to as "Medicaid Income Trusts" or "Miller Trusts." Such trusts also contain a payback provision[xxii] and have limited application because they cannot contain any assets, only income interests.

A "(d)(4)(C)" or "pooled" trust (sometimes referred to as a "C" trust) can only be established for the benefit of an individual who is disabled and must meet the following conditions:

(i) It is established and managed by a nonprofit association;

(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 by section 1382c(a)(3))

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by the parent, grandparent, or legal guardian of such individuals, by such individuals, or by a court; and

(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.

There is no "under 65" requirement with pooled trusts as there is with a (d)(4)(A) trust.[xxiii] However, the In Re Pooled Advocate Trust, Olson, and Lewis, courts concluded that individuals age 65 and older funding a pooled trust could be assessed a Medicaid divestment penalty, just as if they had made an uncompensated transfer to a friend or family member in order to accelerate Medicaid eligibility. The assets within the trust, however, remain excludable assets for Medicaid purposes since the individual has parted with ownership of assets conveyed to the trust.

Nonprofit organizations serving adults with disabilities created pooled trust programs as a way to supplement the individuals' future financial needs. Many of these programs were founded in the 1970s and 1980s. Pooled trust programs lower costs and minimum balances by pooling many irrevocable trust accounts for investment and management purposes. Pooled trust accounts may be funded with the disabled beneficiary's assets; often coming from court awards and settlements or unexpected inheritances.

To conform with state and federal rules, investments of a pooled trust are pooled, but a separate "Sub-Account" is maintained for each beneficiary. Because of this requirement, a single master trust document is shared by all beneficiaries. All beneficiaries must qualify as disabled. The Pooled Advocate Trust, Inc. (PATI) trust itself is restricted to disabled individuals who are South Dakota residents. Persons who may establish a pooled trust are limited to the disabled individual, a court, or the individual's parent, grandparent or guardian. Thus, if the grantor lacks capacity, a court may confirm and establish the trust and approve its funding. A pooled trust is typically funded with the individuals' own funds as first party trusts.

The (d)(4)(A), (d)(4)(B) and (d)(4)(C) trusts balance the interests of the beneficiary with those of the state with the various "payback" requirements and other specific mandatory provisions. These three limited exceptions recognize that public assistance programs like Medicaid do not and cannot meet all the needs of individuals with disabilities, and that trusts which meet the narrow requirements set by Congress should be non-countable resources in order to supplement individuals' needs.

The payback requirement in a pooled trust is qualified. It can be avoided entirely, so long as a deceased beneficiary's trust account is retained by the trust. Distributions to heirs or surviving family members can be made only if the Medicaid agency is repaid in full. In the PATI Trust agreement, the trustee is required to retain all assets in trust for the benefit of other trust beneficiaries if the beneficiary's trust assets are insufficient to repay the Medicaid lien in full. In this situation, a living beneficiary's Sub-Account will receive additional funds by virtue of a deceased beneficiary's Medicaid lien exceeding their remaining Sub-Account balance at the time of death. If the lien can be repaid from the beneficiary's trust account, however, then the Trustee is directed to do this and distribute the remainder to the beneficiary's heirs. The heirs are identified in the joinder agreement completed by the beneficiary or his or her guardian when the trust is initially funded. If the disabled beneficiary never incurred a Medicaid lien, no payback is required and all trust assets can be distributed at death to the beneficiary's heirs.

Third party trusts are those funded with a third party's assets (*e.g.*, parents place assets in trust for their child with a disability). The rules for third-party trusts are quite different than for the three first-party trusts. Most importantly, third-party trusts need not contain a payback provision.[xxiv] Thus, if one funds a trust for the benefit of a disabled nephew, any amounts remaining in the trust at the nephew's death can be distributed to the nephew's siblings without first satisfying a Medicaid lien.

The In re Pooled Advocate Trust case involved a pooled trust first created in 2004 by Pooled Advocate Trust, Inc. (or "PATI"), a tax exempt 501(c)(3) organization. First Premier Bank serves as the trust's trustee. PATI's pooled trust was modeled after others established throughout the country. DSS adopted a policy in 2009 that would treat contributions to the PATI trust as divestments triggering a period of ineligibility if the contributions were made when the disabled individual was age 65 or older. PATI obtained a favorable ruling from Seventh Circuit Court Judge Davis, but DSS appealed.

While the appeal was pending before the South Dakota Supreme Court, two trust beneficiaries (Fred and Gladys Matthews) who had funded Sub-Accounts with the PATI Trust worked their way through the appeal process and eventually had their case consolidated with the PATI case. While the case was pending before the South Dakota Supreme Court, DSS amended its administrative rules to specifically impose divestment penalties for over-65 pooled trust beneficiaries. The Court ultimately decided in favor of DSS and confirmed the over-65 pooled trust divestment penalties rule.

In Olson, the Court first found the nonprofit organization that brought the case had standing to do so in a § 1983 action. This was a favorable ruling, as the Eight Circuit Court rejected the reasoning in a 2009 Tenth Circuit case that concluded Medicaid eligibility rights could not be asserted in a § 1983 action.[xxv] However, the Court found a 2008 letter from CMS to be persuasive authority and sided with the North Dakota Medicaid Agency. The Court said:

> By the omission of an age requirement in [(d)(4)(C) trusts], Congress's intent was to permit disabled persons over age 65 to participate in "C" pooled trusts. In fact, the parties agree that disabled individuals over age 65 can participate in a type "C" pooled trust. North Dakota, however . . . distinguish[es] a temporary disqualification from *participation* in a pooled trust.

The court thus approved North Dakota's over-65 pooled trust divestment penalties rule.

In Lewis, the court also concluded, consistent with the first two cases to weigh-in on the question, that transfers to a pooled trust when the individual is age 65 or older will result in a specific period of Medicaid ineligibility. The Court concluded that certain aspects of Pennsylvania Medicaid law had to be set aside, including a "50% repayment retention provision." The provision required pooled trusts to provide that no more than half of the funds remaining in the beneficiary's Sub-Account could be retained in trust at death, with the remainder subject to a mandatory payback to the State. The Third Circuit ruled this restriction was preempted by federal law. Other than the over-65 aspect of the Lewis Court's opinion, the decision is largely favorable for disability rights advocates.

In view of these decisions, is there still a place for pooled trusts for individuals age 65 and older? Although the funding of a pooled trust for oneself or one's spouse as beneficiary will trigger a divestment penalty for long-term care Medicaid benefits, there are still

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two scenarios where individuals concerned with the prospect of devastating long-term care costs could legally utilize a pooled trust, accelerate Medicaid eligibility, and achieve a measure of asset protection and professional fiduciary management of trust investments. In fact, DSS's Supreme Court Reply Brief in In re Pooled Advocate Trust acknowledged the proper planning opportunities available for protecting an individual's assets, yet qualifying for Medicaid even though the individual might be age 65 or older:

> [T]he pooled trust remains an appropriate option for individuals under the age of 65 as well as those age 65 and older. There is no prohibition against a disabled or elderly individual adding to a pooled trust in which they are a named beneficiary up to age 65. Thereafter, a person may no longer contribute funds to the pooled trust without incurring a transfer penalty, but may continue to benefit from the trust while maintaining Medicaid eligibility. The Department's interpretation of this statute does nothing to nullify the statute or any benefit a disabled or elderly individual may receive from utilizing a pooled trust.

In the first scenario, a disabled over-65 individual could fund a pooled trust and wait at least 60 months prior to making a Medicaid application. So long as the beneficiary avoids submitting a Medicaid application until 60 months after he or she funded a pooled trust, the trust contribution will not result in any adverse Medicaid eligibility consequences. During and after the 60-month period, the Trustee may make discretionary distributions for the beneficiary's benefit, even paying for long-term care expenses if there is not an available public benefit or insurance option to pay for those costs.

In the second scenario, an individual with a disability age 65 or older could consider a pooled trust where it is unlikely he/she could wait out the 60-month look-back period before applying for Medicaid. Here, instead of waiting 60 months, the individual intentionally triggers the divestment penalty by applying for Medicaid immediately after funding the trust. A formula could be utilized:

If **D** > **C** - **I**, then a pooled trust should be considered.

I = Individual's monthly income (social security, pension, etc.)

C = Individual's monthly expenses (care costs, etc.)

D = the Medicaid Divestment Penalty Divisor ($5,204 in 2012)

Stated another way, if the Divestment Penalty Divisor is *greater* than the monthly care costs *less* the individual's monthly income, an older individual may benefit from funding a pooled trust.

For example, assume Betty Jo, age 75, suffers from dementia. She is a widow with $80,000 in assets and $2,000 in monthly income from Social Security and a teacher's pension. She recently entered a nursing home costing $6,000/month. If she does nothing, she will spend down her assets and qualify for Medicaid in about 20 months, leaving her with only $2,000 in assets. Betty Jo could benefit from funding a pooled trust because the Medicaid Divestment Penalty Divisor is greater than her care costs less her income: $5,204 >$6,000-$2,000 ($5,204 is greater than $4,000).

What happens if Betty Jo transferred all but $2,000 to a pooled trust, then applied for Medicaid long-term care assistance? DSS would apply a divestment penalty period of approximately 15 months. During those 15 months, a simple (d)(4)(B) "Miller Trust could funnel her $2,000 monthly income to her care costs, and the Trustee could pay Betty Jo's remaining $4,000 in nursing home bills from her trust Sub-Account. At the end of 15 months, the Trustee would have distributed about $60,000 to pay for nursing home bills, leaving $20,000 in her trust Sub-Account. At that point, the penalty period expires and Betty Jo would qualify for Medicaid. The Trustee could use the remaining $20,000 to supplement her care needs, get her weekly massages or beauty parlor services, engage a care manager to advocate for her best interests, and make her nursing home stay more dignified. If she is on Medicaid for a relatively short period before she passes away, there will still be funds to distribute to her heirs. Otherwise, the funds will be retained in the trust and distributed to other pooled trust beneficiaries. As the South Dakota Supreme Court stated in In re Pooled Advocate Trust:

> DSS' policy does not deny a pooled trust beneficiary Medicaid assistance. The policy merely imposes a mandatory penalty period during which time the applicant is not eligible for long-term care assistance. The applicant may nevertheless qualify for medical-only coverage during the penalty period (as Gladys [Matthews]) did, and after the penalty period expires, the applicant may thereafter be eligible for long-term care assistance.

It is also possible that Betty Jo would pass away, say, six months after funding a pooled trust. In that case, the entire trust balance (except for about $24,000 for six months of care costs) would be distributed to her heirs. There would be no payback or Medicaid lien since she never became Medicaid eligible.

Thus, there may be circumstances where money is preserved both for Betty Jo's supplemental needs and for her heirs. Someone like Betty Jo is really no worse off than they would have been if he/she had done nothing. This is because Medicaid eligibility will be achieved with funds still remaining in the beneficiary's Sub-Account at the expiration of the penalty period if planning is done correctly and costs are accurately projected.

It should also be noted that disabled individuals who are not yet 65 years of age could fund a pooled trust with no divestment penalty or 60-month waiting period. For individuals with disabilities under the age of 65, a pooled trust can result in immediate Medicaid and SSI eligibility because no divestment penalty can be applied. While elder law attorneys across the country see the three recent court decisions as unfortunate and contrary to a closer reading of federal Medicaid rules, disability rights advocates should be aware that appropriate and acceptable planning is still available with pooled trusts, even if the individual is over age 65 when funding the trust.

The author wishes to thank respected South Dakota/Illinois elder law attorney Kristi Vetri (who represented the Matthews in the PATI appeal) for her assistance and editorial suggestions.

[i] In re Pooled Advocate Trust, Inc., 2012 SD 24. In the interests of full disclosure, your author represented Pooled Advocate Trust, Inc. (PATI) and argued the In re Pooled Advocate Trust case before the Honorable Jefferson Davis, Circuit Court Judge, and later the South Dakota Supreme Court. Your author also founded PATI and drafted the PATI trust agreement. See pooledadvocatetrustinc.com.

[ii] Center for Special Needs Trust Administration, Inc. v. Olson, ___ F.3d ___ (8th Cir. 2012).

[iii] Lewis v. Alexander, ___ F.3d ___ (3d Cir. 2012).

[iv] 42 U.S.C. § 1396 *et seq.*

[v] TLC Home Health Care, L.L.C. v. Iowa Dep't of Human Services, 638 N.W.2d 708, 712 (Iowa 2002) (citation omitted).

[vi] Id., citing Madrid Home for the Aging v. Iowa Dep't of Human Services, 557 N.W.2d 507, 511 (Iowa 1996), citing Wilder v. Virginia Hosp. Ass'n, 496 U.S. 498, 502, 110 S.Ct. 2510, 2513 (1990).

[vii] See Sioux Valley Hospital Ass'n v. Lake County, 553 N.W.2d 161 (S.D. 1995).

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Part C Regulations

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line for scheduling a hearing and preparing a decision (availability of witnesses, pending evaluations, exceptional family circumstances, etc.). Therefore, the new regulations allow the hearing officer the discretion to grant a specific extension of time beyond the 30-day timeframe. 34 CFR § 303.437(c).

Due Process Complaint – 34 CFR § 303.441

The notice of the due process complaint, information necessary to be included in the complaint, the lead agency's response to the complaint, and the resolution meeting regulations remain unaltered. The due process complaint must still include the following information: (1) The name of the child; (2) The address of the residence of the child; (3) The name of the EIS provider serving the child; (4) In the case of a homeless child, available contact information for the child, and the name of the EIS provider serving the child; (5) A description of the nature of the problem of the child relating to the proposed or refused initiation or change, including facts relating to the problem; and (6) A proposed resolution of the problem to the extent known and available to the party at the time. 34 CFR § 303.441(b)(1)-(6). The party receiving the due process complaint must, within 10 days of receiving the due process complaint, send to the other party a response that specifically addresses the issues raised in the due process complaint. 34 CFR § 303.441(f).

Resolution Meeting – 34 CFR § 303.442

Within 15 days of receiving the notice of the parent's due process complaint, and prior to the initiation of the due process hearing timeline, the lead agency must convene a resolution meeting. 34 CFR § 303.442(a)(1). The purpose of this meeting is for the parent and lead agency to discuss the due process complaint and potentially resolve the complaint without the need for a hearing. 34 CFR § 303.442(a)(2). The meeting does not have to happen if both parties agree to waive the resolution meeting or if they agree to use mediation. 34 CFR § 303.442(3)(i)-(ii).

The parties have 30 days following the filing of a complaint to resolve the issue. If, after those 30 days, the complaint has not been resolved, the due process hearing may occur. 34 CFR § 303.442(b)(1). If the lead agency has been unable to get a parent to attend a resolution meeting, after the 30-day timeline has run the lead agency may request that the hearing officer dismiss the complaint. If the lead agency has not scheduled a resolution meeting within the 15-day timeframe following the filing of the due process complaint, the parent may request to begin the due process hearing timeline. 34 CFR § 303.442(b)(5). A parent, lead agency, or EIS must request a hearing within two years from the date the parent, lead agency, or EIS knew or should have known about the alleged action which was the basis for the due process complaint. 34 CFR § 303.443(e).

Hearing Rights – 34 CFR § 303.444

All hearing rights guaranteed in the 2004 amendments are mirrored in the 2011 regulations. Any party to a hearing has the right to: (1) Be accompanied and advised by counsel and by individuals with special knowledge or training with respect to the problems of infants or toddlers with disabilities; (2) Present evidence and confront, cross-examine, and compel the attendance of witnesses; (3) Prohibit the introduction of any evidence at the hearing that has not been disclosed to that party at least five business days before the hearing; (4) Obtain a written or, at the option of the parents, electronic, verbatim record of the hearing; and (5) Obtain written or, at the option of the parents, electronic findings of fact and decisions. 34 CFR § 303.444(a)(1)-(5). Parents should receive a copy of the hearing record and the facts and decision at no cost. 34 CFR § 303.444(c)(2).

As mentioned previously, this article covers only the procedural safeguards section of Part C of IDEA. There were a variety of changes made to other sections of the regulations and parents should become familiar with those sections of Part C as well. Other major areas of change include, but not limited to:

- Transition requirements;
- Natural environment provisions;
- IFSP content, including the "early intervention services" and "other services" components;
- Financial responsibility, systems of payment and ability to pay, as well as to the use of public benefits, insurance, and private insurance; and
- Provisions related to monitoring, enforcement, reporting, and allocation.

If you have questions on Part C services or the changes to Part C, please contact South Dakota Advocacy Services. You may also contact the SD lead agency, Birth to 3 Connections, at 800 Governor's Drive, Pierre SD 57501, 605-773-3678, or 800-305-3064.

ACRONYMS USED IN THIS ARTICLE

IFSP – Individual Family Service Plan
LEA – Local Educational Agency
SEA – State Educational Agency
FERPA – Family Educational Rights and Privacy Act
IDEA – Individuals with Disabilities Education Act
EIS – Early Intervention Systems
GEPA – General Education Provisions Act
EDGAR – Educ. Dept. General Administrative Regulations
CFR – Code of Federal Regulations

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[viii] S.D. Admin. R. 67:46:04:14.
[ix] S.D. Admin. R. ch. 67:46:03.
[x] SDCL § 28-1-1.
[xi] 42 U.S.C. § 1396(a)(10)(C)(i)(III).
[xii] See Weatherbee ex rel. Vecchio v. Richman, 2009 WL 3792406 (3d Cir. 2009) (holding that Pennsylvania's attempt to narrow the exemption for certain annuities under federal Medicaid law is void under preemption doctrine).
[xiii] S.D. Admin. R. 67:46:05:06.
[xiv] S.D. Admin. R. 67:46:05:09.
[xv] S.D. Admin. R. 67:46:05:09:02.
[xvi] S.D. Admin. R. 67:46:05:32:01.
[xvii] S.D. Admin. R. 67:46:05:32:02.
[xviii] 42 U.S.C. § 1396p(d)(4)(A)-(C).
[xix] Pub. L. 103-66, *et seq.*; 107 Stat. 312, *et seq.*
[xx] 42 U.S.C. § 1396p(d)(4)(A).
[xxi] 42 U.S.C. § 1396p(d)(4)(B).
[xxii] 42 U.S.C. § 1396p(d)(4)(B)(ii).
[xxiii] 42 U.S.C. § 1396p(d)(4)(C); see also S.D. Admin. R. 67:46:05:32:03(1)-(3).
[xxiv] Harry S. Margolis, ed., The Elder Law Portfolio Series 3-23 (2009).
[xxv] Hobbs v. Zenderman, 579 F.3d 1171 (10th Cir. 2009).