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Decanting SNTs: Preserving SSI Eligibility by Avoiding Early Termination Policy

Amy J. Fanzlaw*

I. INTRODUCTION

Successfully decanting special needs trusts (“SNTs”) requires a rich understanding of trust law and means-tested benefits, but few practitioners are hip-deep in both. No matter how experienced in decanting one may be, preserving eligibility for Supplemental Security Income (“SSI”) and SSI-related Medicaid is simply outside the scope of traditional estate planning. This article discusses how Social Security Administration (“SSA”) will treat decanting self-settled SNTs and suggests ways to avoid losing SSI eligibility in drafting and decanting them.¹

II. SSA AND ITS DECANTING AND EARLY TERMINATION POLICIES

SSA reviews SNTs to determine whether they are countable resources for SSI-eligibility purposes. Depending upon when an SNT is decanted, SSA may also review decanting, either directly or as part of SNT review.² Although decanting has gained immense popularity in the past decade, it has been difficult to anticipate how SSA will treat decanting.

Just as decanting has been on the IRS “no-ruling” list for years,³ SSA had delayed publishing national policy on decanting for years, instead providing only Regional Chief Counsel Precedents (RCCPs) for a glimpse of how SSA approaches decanting self-settled SNTs.⁴

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¹ As used here, “self-settled SNTs” refers to trusts created with a disabled beneficiary’s assets, which must strictly adhere to 42 U.S.C. § 1396p(d)(4)(A) to be valid and recognized as a non-countable resource. Pooled SNTs governed by 42 U.S.C. § 1396p(d)(4)(C) are also self-settled but are different animals and not this article’s focus.

² SSA should be notified within 10 days of decanting if it could affect a current SSI recipient’s trust interest. *See* 20 C.F.R. §§ 416.708(c)-(d), 416.714.

³ *See, e.g.*, Rev. Proc. 2020-3, 2020-1 I.R.B. 131 § 5.01(8), (13)-(14).

⁴ *See* SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), PS 01825.026 MINNESOTA, PT. D. CPM 19-103 SIX STATE SURVEY ON DECANTING STATUTES WITHIN REGION V (Aug. 16, 2019) [hereinafter POMS PS 01825.026], <https://secure.ssa.gov/apps10/poms.nsf/lnx/1601825026> [<https://perma.cc/9P3D-C2NX>]. SSA’s national policies are contained in its Program Operations Manual System (POMS), available only online at <https://secure.ssa.gov/apps10/poms.nsf/partlist>.

RCCPs are legal opinions analyzing how the law would likely be interpreted by courts under certain facts.⁵ They are issued as guidance for SSA regional staff in deciding similar coverage, entitlement, and post-entitlement issues on subsequent claims. In recent years, multiple RCCPs have indicated that when a self-settled SNT contains a decanting clause contemplating the transfer of assets to another trust, SSA must determine whether the clause, “read in light of applicable state law, complies with SSA trust policy, including its rules on early termination of trusts.”⁶ In particular, it was stated that SSA’s “default practice generally is to consider total decanting (i.e., decanting of all trust assets) as a form of early termination and to evaluate a provision for such decanting in a [self-settled] trust against the instructions on early termination.”⁷ In other words, according to the RCCPs, when a self-settled SNT either has a decanting clause or is totally decanted, early termination policy would be applied.

SSA’s early termination policy was developed to address the practice of drafting self-settled SNTs with clauses allowing termination prior to the beneficiary’s death if the beneficiary’s disability ended or the beneficiary otherwise became ineligible for benefits. Such clauses, with nothing more, would allow self-settled SNTs to escape federally imposed obligations to reimburse states that provided Medicaid services to the beneficiary during lifetime. Therefore, early termination policy states that a self-settled SNT with an early termination clause will be a countable resource unless upon termination, all states that provided Medicaid services are reimbursed from trust assets before any other disbursements (except taxes and some administrative expenses) and all remaining funds are distributed to the disabled beneficiary.⁸

⁵ See SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), GN 01010.800 RESOLVING POLICY AND LEGAL ISSUES IN ADJUDICATION (Nov. 10, 2011), <https://secure.ssa.gov/poms.nsf/lnx/0201010800#:~:text=Precedents%20of%20Regional%20Applicability,unless%20superseded%2C%20rescinded%20or%20modified> [<https://perma.cc/4ZTQ-J5A9>].

⁶ POMS PS 01825.026, *supra* note 4, at PT. D. §§ 1, 2; see SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), PS 01825.041 OREGON, PT. B. CPM 19-220 ANALYSIS OF OREGON SPECIAL NEEDS TRUSTS AS AMENDED (Nov. 15, 2019), <https://secure.ssa.gov/poms.nsf/lnx/1601825041> [<https://perma.cc/U37V-GNG2>]; POMS PS 01825.026, *supra* note 4, at PT. C. PS 20-029 REVIEW OF THE FIRST AMENDMENT TO THE 2019 AMENDED AND RESTATED LSS SPECIAL NEEDS POOLED TRUST.

⁷ POMS PS 01825.026, *supra* note 4, at PT. D. § 2 n.11.

⁸ *E.g.*, SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), SI 01120.199 EARLY TERMINATION PROVISIONS AND TRUSTS, PT. E. POLICY FOR EARLY TERMINATION PROVISIONS (Oct. 22, 2020) [hereinafter POMS SI 01120.199], <https://secure.ssa.gov/apps10/poms.nsf/lnx/0501120199> [<https://perma.cc/Z39Z-8SVT>]. A “sole benefit” trust that distributes assets to the beneficiary after a certain age will satisfy the last prong. See *id.* at PT. E. § 1; POMS PS 01825.026, *supra* note 4, at PT. F. PS 18-106 DOES AN EARLY TERMINATION CLAUSE IN A SPECIAL NEEDS TRUST MEET SSA POLICY

SSA's lack of a national decanting policy was problematic. While RCCPs are available to the public, they are so poorly organized that any benefit is limited. They are also inherently limited to a region and not necessarily indicative of national treatment of an issue.

In October 2020, SSA released national policy on decanting, adopting the RCCP view but with some differences.⁹ SSA's national policy broadly defines decanting as "the distribution or transfer of trust property from one trust to one or more other trusts."¹⁰ The policy states that decanting may involve early termination of the first trust or "the effect of decanting may be materially the same as the effect of an early termination."¹¹ Recognizing that decanting is complex and heavily dependent upon state law, review by Regional Chief Counsel may be appropriate to determine whether a decanting provision allows for early termination or should be treated like it does.¹² If so determined, SSA will evaluate the decanting provision¹³ under early termination policy.¹⁴

There is one narrow exception. A self-settled SNT may include a decanting clause without a Medicaid reimbursement clause or otherwise meeting early termination requirements if it allows "solely" for a transfer of the beneficiary's assets to a self-settled SNT for the same benefi-

REQUIREMENTS FOR CONTINUED ELIGIBILITY FOR SSI § 2 (June 28, 2018). Additionally, the beneficiary may not hold the power to terminate, and the SNT must meet all other criteria for a non-countable resource. *See* SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), SI 01110.100 DISTINCTION BETWEEN ASSETS AND RESOURCES, PT. B. POLICY PRINCIPLES (Jan. 21, 1993), <https://secure.ssa.gov/apps10/poms.nsf/lnx/0501110100> [<https://perma.cc/EA9H-U6PR>]; SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), SI 01120.200 INFORMATION ON TRUSTS, INCLUDING TRUSTS ESTABLISHED PRIOR TO JANUARY 01, 2000, TRUSTS ESTABLISHED WITH THE ASSETS OF THIRD PARTIES, AND TRUSTS NOT SUBJECT TO SECTION 1613(E) OF THE SOCIAL SECURITY ACT, PT. D. POLICY FOR TRUSTS AS RESOURCES (June 7, 2018) [hereinafter POMS SI 01120.200], <https://secure.ssa.gov/apps10/poms.nsf/lnx/0501120200> [<https://perma.cc/2QF2-PUZQ>].

⁹ *See* POMS SI 01120.199, *supra* note 8.

¹⁰ *See id.* at PT. D. DEFINING TERMS FOR TRUSTS § 7. The definition is not limited to the exercise of trustee authority under a decanting statute or traditional trust decanting clause so it is somewhat concerning that other types of distributions might inadvertently fall into this broad definition.

¹¹ *Id.*

¹² *See id.*

¹³ SSA does not distinguish between decanting provisions in trusts and statutory decanting provisions, and portions of the policy do, at different times, refer to each, but presumably, the decanting policy applies only to decanting clauses in trusts. If it were to also apply to decanting statutes, every self-settled SNT situated in a jurisdiction with a decanting statute must comply with early termination policy, which would be a preposterous result.

¹⁴ *See id.*

ary.¹⁵ To qualify for this exception, the decanting clause must contain “specific limiting language” precluding “disbursements” other than to another self-settled SNT for the same beneficiary or to pay certain administrative expenses.¹⁶ Presumably, the beneficiary must also be under age 65 at the time of transfer.¹⁷

This exception is the most obvious difference between the RCCP view and the national decanting policy. While there is at least one RCCP approving an early termination clause directing a self-settled SNT to a second trust for the sole benefit of the beneficiary rather than outright to the beneficiary,¹⁸ this exception in the decanting policy is the first time SSA has specifically authorized decanting from a self-settled SNT to another self-settled SNT in lieu of complying with early termination policy.

One less obvious difference between the RCCP view and the national decanting policy is that it appears early termination policy will not be routinely applied each time a self-settled SNT includes a decanting clause, although this does not mean that decanting clauses are necessarily “safe” to include in all self-settled SNTs. It also seems that early termination policy could be applied even when a self-settled SNT is partially decanted as opposed to totally decanted. Therefore, decanting less than all trust corpus is not automatically safe, either.

As a result of SSA releasing its national policy on decanting, drafting and decanting SNTs will be significantly affected. Strict adherence to early termination policy is difficult and can be tricky. If SSI is denied due to a departure from early termination policy, or if SSA erroneously applies early termination policy, relief comes, if at all, only after lengthy and costly appellate proceedings. The better practice is to reduce the likelihood that SSA will apply the policy.

¹⁵ See *id.* at PT. E. § 2. The trust may be either another self-settled SNT meeting the requirements of 42 U.S.C. § 1396p(d)(4)(A) or a pooled SNT meeting the requirements of 42 U.S.C. § 1396p(d)(4)(C).

¹⁶ See *id.* The use of “disbursements” without any qualifiers seems overly broad, as it would appear to prevent outright distributions to the beneficiary as part of the decanting transaction, which seems nonsensical considering trustees of self-settled SNTs generally enjoy broad distribution powers. To avoid this illogical application, any distribution to or for the benefit of a beneficiary contemporaneous with decanting should be deliberately distinct from the decanting transaction.

¹⁷ By federal law, SSI beneficiaries age 65 or older may not establish self-settled SNTs or pooled SNTs without penalty. See 42 U.S.C. § 1396p(d)(4)(A), (C).

¹⁸ See POMS PS 01825.026, *supra* note 4, at PT. C. This view was adopted in the recent revisions to POMS SI 01120.199, *supra* note 8, at PT. E. § 2.

III. AVOIDING APPLICATION OF EARLY TERMINATION POLICY

A. Decant to Modify (and Keep the TIN)

SSA's policy on decanting fails to provide a bright-line rule on when early termination policy will be applied to decanted self-settled SNTs. Instead, SSA says it will apply early termination policy not only if decanting terminates the trust early, but also if the effect of decanting is materially the same as early termination.¹⁹ This creates uncertainty when decanting. If benefits must be repaid as a result of decanting, then a large portion of an SNT could be depleted immediately, making decanting risky. To help avoid this uncertainty, regardless of whether decanting pursuant to statute or trust clause, approach and effectuate decanting as a modification of the trust rather than a distribution from it because the approach that is taken—whether modification or distribution—will likely determine whether early termination policy will be applied and whether SSI eligibility could be affected.

Traditionally, decanting has been viewed only as an extension of the trustee's distribution power.²⁰ However, there is little (if any) definitive authority for whether decanting, exercised purely as a distribution power, terminates or continues the decanted trust, so if the trust is distributed in its entirety, it is unclear whether a different taxpayer identification number ("TIN") must be obtained and a final Form 1041 for the trust filed.

In 2015, the Uniform Trust Decanting Act clarified this issue. The UTDA views decanting either as a power to distribute some or all assets to a second trust or as a power to modify trust terms.²¹ If decanting is approached as a distribution and all trust corpus is distributed to a second, separate trust with a different TIN to distinguish it as a separate taxpayer, then the first trust is terminated.²² If, however, decanting is approached as a modification and the first trust is either amended in part or restated in whole, the trust remains the same entity and is not terminated.²³ In short, how the trustee or other authorized fiduciary effectuates decanting dictates whether the trust is treated as terminated.

¹⁹ POMS SI 01120.199, *supra* note 8, at PT. D. § 7.

²⁰ See Stewart E. Sterk, *Trust Decanting: A Critical Perspective*, 38 CARDOZO L. REV. 1993, 2000-03 (2017).

²¹ UNIF. TR. DECANTING ACT § 2 cmt. (UNIF. L. COMM'N 2015).

²² *Id.* Of course, if less than all assets are distributed, termination is a non-issue, at least from a trust administration perspective, because the first trust remains funded. Note, however, that partial distribution may still be an issue under the SSA decanting policy if the effect of decanting is materially the same as termination.

²³ *Id.*

The UTDA is barely past toddler stage. Yet of the thirty states with decanting statutes, roughly one-third have adopted the UTDA.²⁴ Other states seem to borrow heavily from some UTDA principles and concepts, stopping somewhere short of wholesale adoption.²⁵ The trend toward the UTDA view is unmistakable, and as this trend continues, state law addressing decanting as either a modification or a distribution should become more developed. Because SSA applies state trust law and generally views trust modification favorably provided state law is followed,²⁶ if a self-settled SNT is decanted in a UTDA jurisdiction—or another state with similar law—and the trustee’s actions evidence that decanting modified the SNT, then SSA should neither treat decanting as a distribution nor apply early termination policy. Even in a non-UTDA jurisdiction, where state law has not explicitly recognized decanting as a modification, taking every action consistent with decanting as a modification is still the better bet than approaching decanting as a distribution.

Therefore, whether decanting pursuant to a clause or statute, all actions by the trustee should be consistent with continuing, not terminating, the SNT after decanting to the extent possible. Rather than securing a new TIN to distinguish the trust after decanting as a separate entity and filing a final income tax return for the decanted trust, consider using the same TIN after decanting, absent a compelling concern that decanting is an income-taxable event that would make starting the statute of limitations by filing a final return desirable.²⁷ To be consistent with trust modification, the product of the decanting should be either the first trust as amended or even a complete restatement of the first

²⁴ The UTDA has been adopted in Alabama (ALA. CODE § 19-3D-1 (2020)), California (CAL. PROB. CODE § 19501 (West 2020)), Colorado (COLO. REV. STAT. § 15-16-901 (2020)), Illinois (760 ILL. COMP. STAT. 3/1201 (2020)), New Mexico (N.M. STAT. ANN. § 46-12-101 (2020)), North Carolina (N.C. GEN. STAT. § 36C-8B-1 (2020)), Virginia (VA. CODE ANN. § 64.2-779.1 (2020)), Washington (WASH. REV. CODE § 11.107.010 (2020)), and West Virginia (W. VA. CODE § 44D-8B-1 (2020)), and was recently introduced in Massachusetts (S. B. 896, 191st Gen. Ct., Reg. Sess. (Mass. 2019)), and Nebraska (Legis. B. 902, 106th Legis., 2d Sess. (Neb. 2020)).

²⁵ See, e.g., FLA. STAT. § 736.04117 (2020).

²⁶ See, e.g., *supra* text accompanying note 7; SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), SI 01120.202 DEVELOPMENT AND DOCUMENTATION OF TRUSTS ESTABLISHED ON OR AFTER 01/01/00, PT. A. PROCEDURE FOR TRUST DEVELOPMENT § 1 (Oct. 31, 2017), <https://secure.ssa.gov/apps10/poms.nsf/lnx/0501120202> [<https://perma.cc/KHT6-FH6X>]; SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), SI 01120.203 EXCEPTIONS TO COUNTING TRUSTS ESTABLISHED ON OR AFTER JANUARY 1, 2000, PT. C. POLICY FOR SPECIAL NEEDS TRUSTS ESTABLISHED UNDER SECTION 1917(D)(4)(A) OF THE ACT ON OR AFTER DECEMBER 13, 2016 § 7 (July 26, 2018), <https://secure.ssa.gov/poms.nsf/lnx/0501120203> [<https://perma.cc/3258-A9M8>].

²⁷ For federal income tax purposes, a new TIN may be required when trust terms are not substantially similar. See, e.g., PLR 200607015 (Feb. 17, 2006).

trust, using the same name so that trust property need not be retitled.²⁸ If a change of name is preferred, simply report the change of name on the next Form 1041.²⁹ The more that every step of decanting is consistent with modification, the more likely that SSA will view decanting as a modification and not apply early termination policy.

B. Avoid Decanting Clauses

Decanting clauses are often drafted into trusts, even in jurisdictions with decanting statutes, on the belief they help, not hurt, but decanting clauses in self-settled SNTs invite close scrutiny that could jeopardize the beneficiary's SSI eligibility. SSA's policy on decanting is to evaluate all decanting clauses in self-settled SNTs to ensure they do not violate early termination policy.³⁰ One of the most obvious ways to avoid SSA's scrutiny is to avoid decanting clauses, both in drafting and decanting SNTs, when feasible.

Drafting decanting clauses in SNTs to address unforeseen issues is most tempting in states without decanting statutes, and understandably so, as decanting generally requires neither court involvement nor beneficiary participation, which can be more attractive than judicial modification.³¹ However, states without decanting statutes are unlikely to have settled state law that decanting does not terminate the first trust, particularly when so few states have even considered common law decanting,³² and without that, there is little impediment to SSA strictly applying early termination policy. Therefore, decanting clauses in these jurisdictions should comply with early termination policy in all respects. Alternatively, consider options other than decanting clauses, such as allowing change of situs to a jurisdiction with a decanting statute or giving a trust protector the limited power to amend in order to infuse flexibility similar to that which decanting provides.

Decanting clauses in SNTs in states with decanting statutes may be equally risky. Decanting statutes are rarely, if ever, mandatory provi-

²⁸ See UNIF. TR. DECANTING ACT § 2 cmt. (UNIF. L. COMM'N 2015). The "restatement" could be executed by the decanting trustee or another person as the nominal settlor.

²⁹ See, e.g., PLR 200736002 (Sept. 7, 2007). Although self-settled SNTs are grantor trusts, reporting income directly on a Form 1040 is not always done, most often to avoid SSA confusing taxable income with SSI income concepts.

³⁰ POMS SI 01120.199, *supra* note 8, at PT. D. § 7.

³¹ Cf. UNIF. TR. DECANTING ACT Prefatory Note (judicial and non-judicial modification). Beneficiary involvement in SNT modification is ill-advised because it can be interpreted as control over trust corpus, which renders an SNT a countable resource. See POMS SI 01120.200, *supra* note 8.

³² See GEORGE GLEASON BOGERT ET AL., *BOGERT'S THE LAW OF TRUSTS AND TRUSTEES*, ch. 27, § 567 (2020).

sions of trust codes, so trust terms will generally control and override provisions of a decanting statute. Unless the decanting clause strictly complies with early termination policy or strictly adheres to the exception of allowing only a transfer from one self-settled SNT to another for the sole benefit of the beneficiary, inserting a decanting clause in a self-settled SNT will jeopardize SSI eligibility. If drafting an SNT situated in a state with a decanting statute, there should be no reason to take this risk.

The one place early termination policy should not be an issue is third-party SNTs because early termination policy applies only to self-settled SNTs.³³ However, SSA frequently confuses self-settled and third-party SNTs. Decanting and early termination policy are both such complex issues that SSA may erroneously apply the policy to third-party SNTs as well. Therefore, including a decanting clause in any SNT—self-settled or third-party—should give the drafter pause.

In short, decanting clauses should be avoided in SNTs unless there is no suitable alternative and then only after all risks are weighed. If they are included, strict adherence to early termination policy is advised.

C. Explore Other Alternatives

Decanting is a useful tool but not a panacea.³⁴ Other options may be better suited to self-settled SNTs.

One option is to simply distribute most (not all) trust assets outright to the beneficiary, who then establishes a new self-settled SNT. The beneficiary might lose SSI eligibility in the month of distribution,³⁵ but that cost may be acceptable, particularly if the SNT is large.³⁶ Because the beneficiary would be creating a new self-settled SNT, the beneficiary must be under age 65 when the second trust is established and fully funded.³⁷

³³ See POMS SI 01120.199, *supra* note 8, at pt. E. Unlike self-settled SNTs, third-party SNTs need not have reimbursement clauses even upon the beneficiary's death, so no reimbursement is required if the SNT is terminated early.

³⁴ Sterk, *supra* note 20, at 2037.

³⁵ If distribution and funding were completed in the same month, waiver of the one-month SSI overpayment could be requested, thus preserving eligibility. See SOC. SEC. ADMIN., PROGRAM OPERATIONS MANUAL SYSTEM (POMS), SI 02260.030 IMPEDE EFFECTIVE OR EFFICIENT ADMINISTRATION OF TITLE XVI OF THE ACT (ADMINISTRATIVE WAIVER), PT. B. POLICY FOR ADMINISTRATIVE WAIVER (Apr. 4, 2016), <https://secure.ssa.gov/poms.nsf/lnx/0502260030> [<https://perma.cc/R7PQ-3MGJ>].

³⁶ Any concern of the trustee regarding breaching fiduciary duty through this type of distribution could be alleviated by indemnification agreements from the beneficiaries and service of a trust accounting.

³⁷ See 42 U.S.C. § 1396p(d)(4)(A).

Other options include distributing assets to a pooled SNT³⁸ or judicially modifying the SNT instead of decanting.

IV. CONCLUSION

SSA's national policy on decanting has been long awaited. While some uncertainties remain, exercising care when drafting and decanting SNTs helps ensure SSI eligibility will not be inadvertently jeopardized.

³⁸ *See id.* § 1396p(d)(4)(C). Pooled SNTs have the same age-65 requirement as self-settled SNTs so this is not an option for SSI beneficiaries age 65 or older and for recipients of state Medicaid programs absent a state exception.

