

Breakout Session: STATE TRUST LAW ISSUES IN AN ELDER LAW PRACTICE

*Presented by : Bob Mason, CELA, CAP
Founder, TrustChimp*





Does Medicaid preempt state trust law?

Can state law be used to achieve tax objectives?

What state trustee powers can cause problems



State creditor protection laws a concern?

Validity of trust under state law

Case law: Roadmap of road hazards



Partial checklist

**Using UNIFORM Acts
– You’ll need to check
your state**



State Law Applicability



STATE LAW APPLICABILITY

Tales from the Crypt



Doherty v. Director

FACTS

- IIOT
- Trust termination
- P & I determinations
- Special Power
- Retained Residence Right



STATE LAW APPLICABILITY

Tales from the Crypt



Doherty v. Director DECISION

- “Under any circumstances” applied
- “Maximum flexibility” to meet Muriel’s needs



STATE LAW APPLICABILITY

Tales from the Crypt



Doherty v. Director LESSONS

- Lock-in P & I
- Careful of trust terminations
- Subject residence to lease?



STATE LAW APPLICABILITY

A Little History

Pre-OBRA '86

- **State law applied as with any self-settled trust**
- **To extent distributions could be made**



STATE LAW APPLICABILITY

A Little History

OBRA '86

- **Medicaid (DIS)Qualifying Trust**
- **To extent distributions (using **MAXIMUM** discretion) could be made**
- **Trigger trust**



STATE LAW APPLICABILITY

A Little History

OBRA '93

- **The scheme we all know and love**
- **The “UNDER ANY CIRCUMSTANCES” Test**



STATE LAW APPLICABILITY

A Little History

OBRA '93

“UNDER ANY CIRCUMSTANCES”

State considerations such as:

- ***Purposes of creation***
- ***Existence of trustee discretion***

To be disregarded



STATE LAW APPLICABILITY

A Little History

OBRA '93
Other than that

State law applies



TRUST CREATION Capacity

UTC § 402: Rev Trust = Will



TRUST CREATION Capacity

Irrev Trust = Higher

**Gift/Contractual Equivalent:
Understands Nature, Scope and Effect**

Void or Voidable?

Tough call for the attorney



TRUST CREATION

Creation by Agent

What does your state say?

Revocable versus Irrevocable



TRUST CREATION

Creation by Agent

**UTC gives authorized agent power to
revoke or amend a REVOCABLE Trust
If expressly authorized –
Otherwise silent**

Some states give power to create



TRUST CREATION

Creation by Agent

UPOAA § 201:

IF AUTHORIZED, AIF may “create, amend, revoke, or terminate an inter vivos trust”



ASSET PROTECTION

Creation by Agent

UPOAA § 201 Official Comment:

Grant of authority must be specific



TRUST CREATION

Creation by Agent

Dishman v. Dougherty
(2015 Kentucky Appeals)



TRUST CREATION

Creation by Agent

**States with BOTH UTC and UPOAA:
Should be no problem**

States with UTC but NO UPOAA?

**Worth checking neighboring state?
UTC § 403**



ASSET PROTECTION ISSUES

Spendthrift Clauses



**Insure your trusts
contain one!**

**POMS (SSI): [Beneficiary's] “ability to direct”
... depends upon agreement or state law
“(it contains a valid spendthrift clause)”**



ASSET PROTECTION ISSUES

Fraudulent Conveyance

Who'll
even know,
baby?

Transfers that:

- **Leave insolvent, and**
- **With intent to hinder, delay, or defraud**





ASSET PROTECTION ISSUES

Fraudulent Conveyance

Who'll
even know,
baby?

Medicaid issues?

- **Nah!**

Private creditors

- **You bet!**





ASSET PROTECTION ISSUES

Fraudulent Conveyance

Who'll
even know,
baby?

Bottom Line with Irrev Trust:

- **Either make sure Medicaid eligible, OR**
- **Have a funding mechanism**

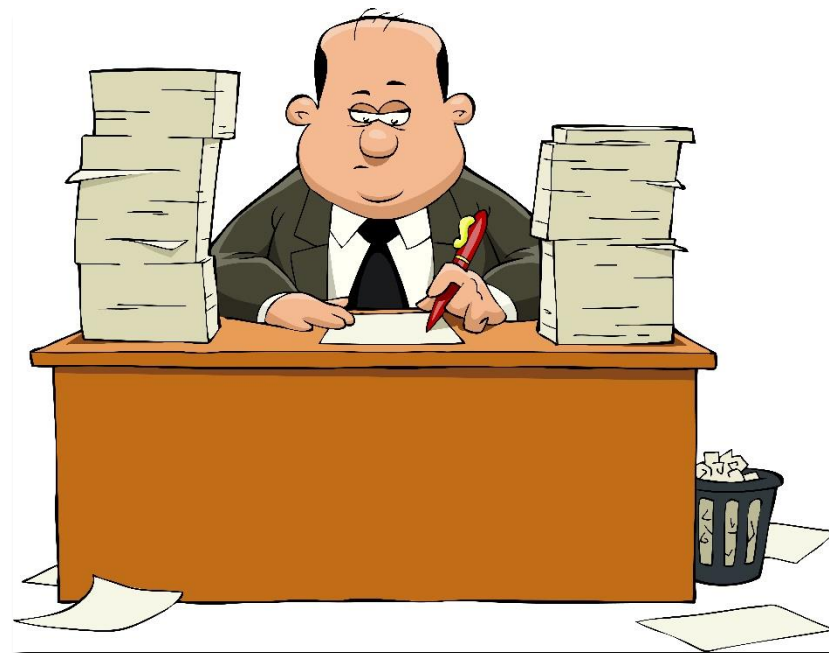




ADMINISTRATION ISSUES

Principal and Income Act

Watch the
boilerplate and
incorporation by
reference



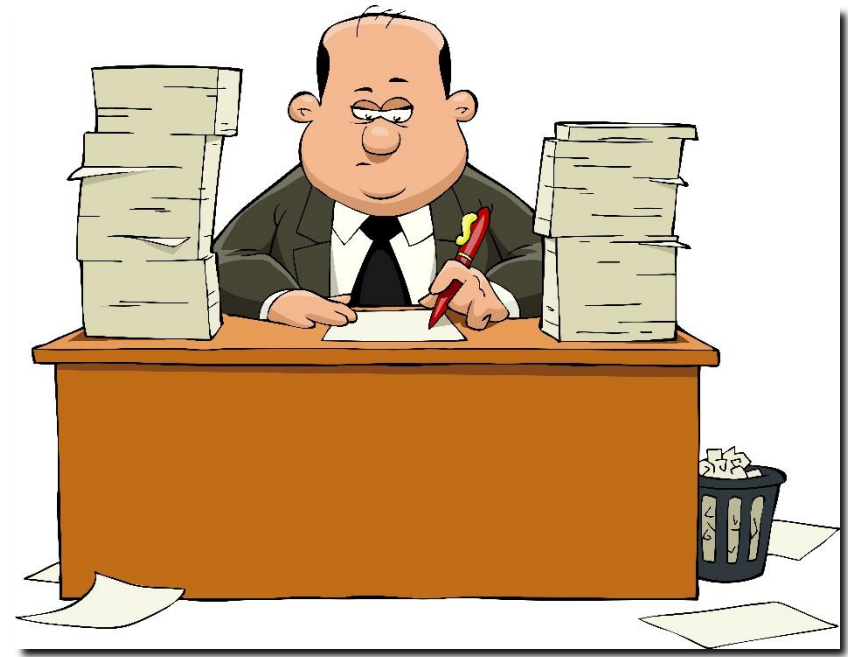
*Lessee . . . Principal to the right,
income to the left*



ADMINISTRATION ISSUES

Principal and Income Act

What about (d)(3)(B)(i)
“any circumstances”
and . . .
Trustee’s call on
Principal and Income?



Dang! I coulda been an actuary



ADMINISTRATION ISSUES

Principal and Income Act



HINT: Consider sticking with the statute and avoiding discretion



ADMINISTRATION ISSUES

Prudent Investor Act



UPrIA § 3:

**Duty to diversify . . .
BUT . . . “Circumstances
can overcome”**

BUT: An express relief from duty can be a relief when family goes nuclear



ADMINISTRATION ISSUES

Decanting

**UTDA adopted in 2 states
and introduced in 3**

**Many other states have
“custom” statutes**

**UTDA § 13 “changed
circumstances” and
disability hypo**





ADMINISTRATION ISSUES

Situs Change



I got Delaware on my mind!

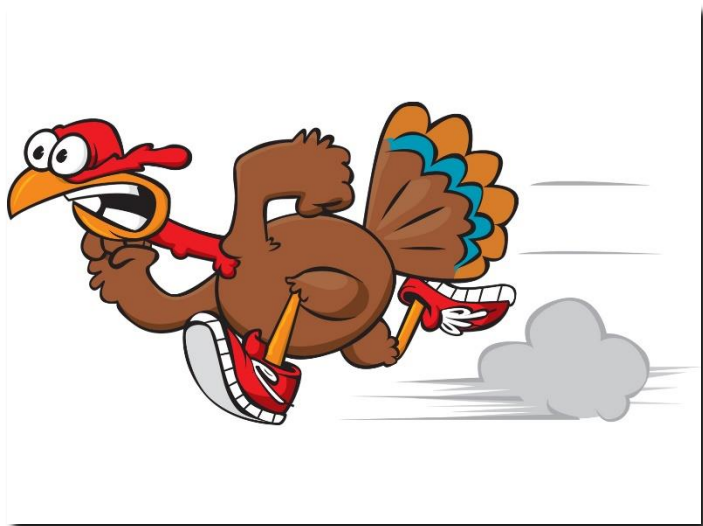
UTC § 108:

Duty to administer “at a place appropriate to its purposes”



ADMINISTRATION ISSUES

Situs Change



I got Delaware on my mind!

Reasons:

- **State tax**
- **Favorable decanting**
- **Minimizing admin
\$\$**
- **Creditor protection**
- **Streamlined
mod/term process**



TAX ISSUES



**Main intersection of
state law and tax:**

Capital Gains



TAX ISSUES



The Problem:

**INDIVIDUALS UNDER
\$418,500 – 15%**

TRUSTS OVER \$12,500 – 20%



TAX ISSUES

Insult to Injury: Net Investment Income Tax



**INDIVIDUALS OVER \$200,000
(MARRIED OVER \$250,000)**

TRUSTS LESSER OF 3.8% OF:

- **UNDISTRIBUTED NET INVESTMENT INCOME**
OR
 - **AGI - \$12,500**



TAX ISSUES

Insult to Injury: Net Investment Income Tax

THE PROBLEM FOR TRUSTS:

**FOR A TRUST AT JUST \$12,500:
CAPITAL GAINS TAXED AT 23.8%**





TAX ISSUES

PRINCIPAL



PRINCIPAL



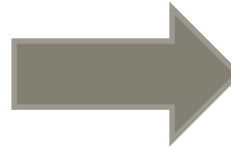
Capital Gains

**Sale of capital asset represents
conversion of an asset from tangible
asset to fungible cash**



TAX ISSUES

PRINCIPAL



PRINCIPAL



Capital Gains

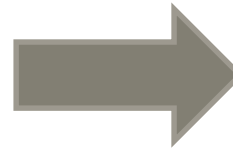
Default setting: Capital Gains allocated to Principal

Both State and Tax law track this concept



TAX ISSUES

PRINCIPAL



PRINCIPAL



Capital Gains

DNI: Determines what income remains in trust and what deemed distributed to beneficiaries



TAX ISSUES

Exceptions?

Can State Law Help?

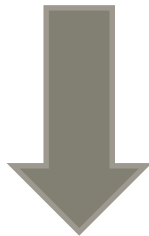


Beneficiary
From
Hell



TAX ISSUES

PRINCIPAL



Capital Gains

EXCEPTIONS!

**Consider In-kind Distribution,
THEN Sell**

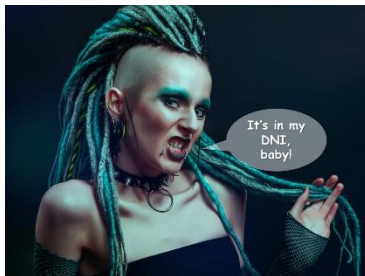
BUT ...

You'll need authorization



TAX ISSUES

PRINCIPAL



EXCEPTIONS!

- Trust Agreement?
- State Law?
 - UTC § 816(22) not helpful (distributions methodology)
 - Incorp by ref statute?



Capital Gains



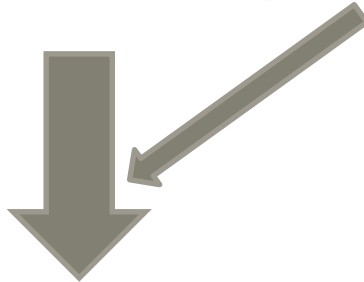
TAX ISSUES

PRINCIPAL



Capital Gains

**Discretionary
Distribution**



EXCEPTIONS!

- **If Agreement or State P&I allows*, AND**
- **As long as Trustee does it CONSISTENTLY**

***UTC not helpful; Check your state**



TERMINATION ISSUES

UTC § 411 Mods or Terminations



411(a):

- **Upon consent of settlor and all beneficiaries with no court supervision**
- **Even if inconsistent with material purpose**
- **Distributed “as agreed by the beneficiaries”**



TERMINATION ISSUES

UTC § 411 Mods or Terminations



411(b):

- **Upon consent of all beneficiaries**
- **If court finds NOT inconsistent with material purpose**
- **Distributed “as agreed by the beneficiaries”**



TERMINATION ISSUES

Mods or Terminations



Once again, 1396p(d)(3)(B) “Any circumstances”

UTC § 105 generally allows “overwrites” in trust

Maybe clarify who gets what if terminates?



TERMINATION ISSUES

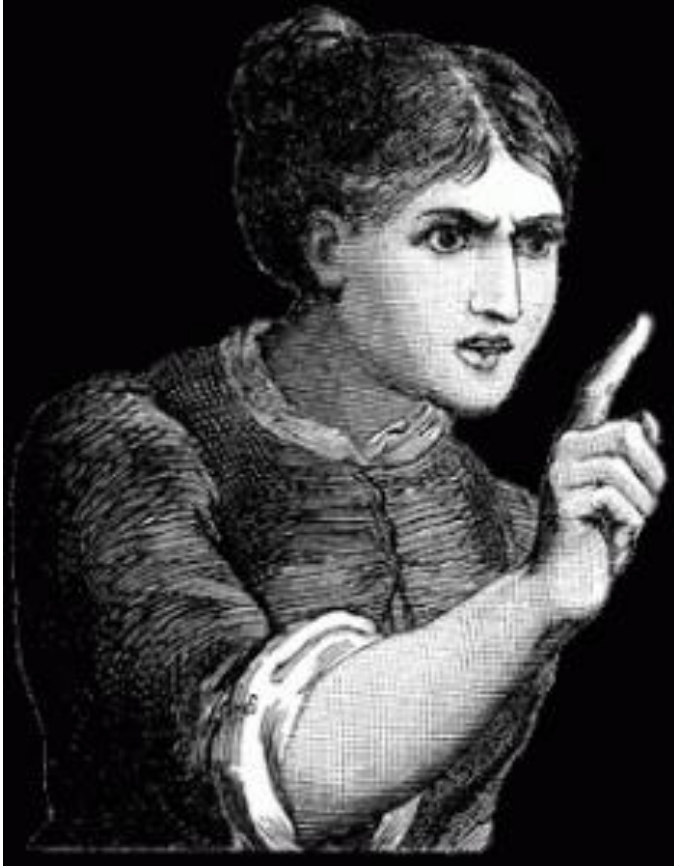
Revocable Trusts

REVOKED

UTC § 602: AIF may revoke if authorized

Some states tighter

(NC: Only if beneficiaries remain unchanged)



- **Know your state's laws**
- **Join me in cursing boilerplate**



WANT TO LEARN MORE ABOUT PUBLIC BENEFITS AND TRUSTS?

- 1. Grab a free membership at
TrustChimp.com**
- 2. Go take a sneak peek at The BaseCamp**



Download these slides at:

www.TrustChimp.Com/boston