

## **Drafting Irrevocable Medicaid Trusts after the Doherty Decision**

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### **Procedural History:**

The individual's application for MassHealth was denied at a Fair Hearing. The Superior Court upheld the Decision of MassHealth on February 29, 2008 (Welch, J.). The Massachusetts Appeals Court upheld the Superior Court ruling on June 19, 2009.

### **Facts:**

On July 18, 1981, Mr. and Mrs. Doherty established the William A. Doherty and Muriel S. Doherty Family (Revocable) Trust. Mr. Doherty died in December, 1987 and subsequently, on April 12, 2000, Mrs. Doherty amended and restated the trust changing its name to the "Muriel S. Doherty Irrevocable Trust." In addition to making the trust irrevocable, Mrs. Doherty resigned as the Trustee but remained the sole Settlor. Her niece and nephew, James D. Doherty, Jr. and Sheila M. Doherty, respectively, were listed as the Trustees. The trust assets were worth approximately \$631,000 and the trust income annually was approximately \$27,000.

### **Statutory Framework:**

Medicaid trusts are governed by 42 U.S.C. §1396(p)(D)(3)(B), which states:

"(i) if there are any circumstances under which payment from the trust could be made to or for the benefit of the individual, the portion of the corpus from which or the income on the corpus from which, payment to the individual could be made, shall be considered resources available to the individual, and payments from that portion of the corpus or income, (I) to or for the benefit of the individual shall be considered income of the individual, and (II) for all other purposes shall be considered a transfer of assets by the individual subject to a look back period."

The Massachusetts Regulation 130 CMR 520.023(C)(1)(C)(a), states:

"In the case of a self-settled trust... any portion of the principal or income from the principal, such as interest of an irrevocable trust, that could be paid under any circumstances to or for the benefit of the individual, is a countable asset."

The Supreme Judicial Court in Cohen v. Commissioner of the Division of Medical Assistance, 423 Mass. 299 (4/13/1996), addressed these sections and determined that the federal statute should be strictly construed and has taken the position that "any circumstances" as outlined in the statute to mean "maximum amount capable of distribution under a trust is deemed to be an available resource of the beneficiary, regardless of whether the trustee actually exercises his or her discretion (to distribute funds)." In Cohen and its companion cases, the trusts in question were so-called "trigger" trusts, meaning the ability of the trustee to pay income and/or principal to or for the benefit of the settlor terminated upon either an event such as institutionalization or

upon time. In all such cases, the assets were deemed to be fully countable (regardless of the lapse of time and/or the happening of the circumstance).

<b>Trust Provisions</b>	<b>Superior Court Analysis</b>	<b>Appeals Court Analysis</b>
<p><b>Article II of Family Trust:</b></p> <p>The purpose of this Trust is to supplement, but not to supplant, what benefits and services the Settlor may from time to time be eligible to receive by reason of her age, disability or other factors from federal, state, and local government, insurance and charitable sources. This Trust is established with the recognition that the nature and extent of the complex and multiple needs of the Settlor are such that her own resources and those of her family, would quickly become exhausted if relied upon as a primary resource of her care. It is recognized further that governmental and charitable programs, in themselves, contain many gaps which, if not addressed, would greatly reduce the possibility of the Settlor maintaining herself as independently as possible and having the capacity to meet her future needs adequately for medical, residential, personal, and other services. With these considerations guiding its decision-making, the Trustee agrees to take control and management of the Trust estate, and invest and reinvest the principal, receive the income therefrom, and, after paying the reasonable and proper expenses of the Trust, manage and distribute the principal and net income of the Trust in accordance with the requirements of this instrument.</p> <p>Without limiting or enlarging the authority of the trustee in accordance with the trust purposes, it is stipulated that the Trust shall be used in ways that will best enable the Settlor to lead as normal, comfortable, and fulfilling life as possible; in fact, regardless of the future health status, she be cared for at home or in any event in the most normal and home-like environment as possible and consistent with her needs for treatment and care; that she may have as many opportunities as possible for normal social interaction with members of her family and other persons in the community in a manner consistent with her age and interests; and that she have every reasonable opportunity to be responsible for her own welfare, independent of this Trust, to the extent of her capacities.</p>	<p><b>Article II of Family Trust:</b></p> <p>Article II establishes that the Family Trust was established for Doherty’s benefit and urges the Trustee to accumulate principal to better meet her future needs.</p>	<p><b>Article II of Family Trust:</b></p> <p>We remain unconvinced that the niece and nephew are unable, in any reasonably foreseeable circumstance, to invade trust assets for Muriel’s benefit. When considered as a whole, what strikes us most strongly is that Muriel’s trust constitutes a remarkably fluid vehicle intelligently structured to provide both Muriel and the trustees maximum flexibility to respond to Muriel’s changing life needs. Indeed, embedded in the trust governing recitation is not only an explicit assessment that public or other charitable benefits will likely be insufficient to provide Muriel the quality of life she might desire, but the corollary implicit direction for the trustees, in such case, to invade assets to make up that difference.</p>

<b>Trust Provisions</b>	<b>Superior Court Analysis</b>	<b>Appeals Court Analysis</b>
<p>The Trustee shall accumulate the trust principal to the extent feasible due to the unforeseeability of the Settlor’s future needs, however, accumulation or use of Trust is to be determined without regard to the interests of the remaindermen.</p>		
<p><b>Article V. A. 1.: Net Income</b></p> <p>The Trustee shall pay the entire net income from the family trust to or for the benefit of the Settlor in quarterly or more frequent installments during her lifetime.</p>	<p><b>Article V. A. 1.:</b></p> <p>No problem – Income is available</p>	<p><b>Article V. A. 1.:</b></p> <p>No Problem – Income is available</p>
<p><b>Article V. A. 2.: Distributions of Principal</b></p> <p>During the lifetime of the Settlor, the Trustee shall make no distributions of principal from the family trust to or on behalf of the Settlor.</p>	<p><b>Article V. A. 2.: Distributions of Principal</b></p> <p>Article V. A. 2. purports to prohibit the trustee from distributing trust principal to Doherty stating, “During the lifetime of the Settlor, the Trustee shall make no distributions of principal from the family trust to or on behalf of the Settlor.” The Superior Court quotes, “This provision, however, is in direct conflict with many of the provisions of the trust, citing Article II, which establishes that the Trust was created for the benefit of Doherty to accumulate principal, Article V. C., which requires the Trustee to obtain Doherty’s permission before selling the Chestnut Street property, Article IV. giving Doherty the right to assign principal through an instrument during her lifetime or by Will to family members of a choice, <u>and finally, Article XXII, giving the Trustee the unfettered discretion to close the family trust and distribute all the assets to the beneficiaries.</u></p>	<p><b>Article V. A. 2.: Distributions of Principal</b></p> <p>The Appeals Court did not address the lifetime power to appoint nor did it address the testamentary power to appoint. The Appeals Court wrote, “We observe that, pursuant to Article XXII, the Trustee may, in its sole discretion and notwithstanding anything contained in this Trust to the contrary, pay over and distribute the entire principal of the trust fund to the beneficiaries thereof, free of all trusts, so long as the trustees in their sole judgment determine that the fund created shall at any time be of a size which... shall make it inadvisable or unnecessary to continue such trust fund.”</p> <p>The Appeals Court also focused on Article XIV. H., which gives the trustee to determine all questions as between income and principal and to credit or charge to income or principal or to a portion between them, any receipt or gain. Notwithstanding any statute or rule of law for distinguishing income from principal or any determination of the courts.</p>
<p><b>Article IV: Lifetime Power of Appointment:</b></p> <p>Article IV. granted Doherty the right to assign principal, through an instrument during her lifetime, to members of her choice.</p>	<p><b>Article IV:</b></p> <p>Problematic when combined with all other “bad” provisions.</p>	<p><b>Article IV: Power of Appointment:</b></p> <p>Did not discuss.</p>

<b>Trust Provisions</b>	<b>Superior Court Analysis</b>	<b>Appeals Court Analysis</b>
<p><b>Article V: Testament Power of Appointment:</b></p> <p>Article V. granted Doherty the right to assign principal through an instrument, by Will, to family members of her choice.</p>	<p>Problematic when combined with all other “bad” provisions.</p>	<p>Did not discuss.</p>
<p><b>Article XXII:</b></p> <p>Article XXII gives the trustee the unfettered discretion to close the family trust and distribute all assets to the beneficiaries.</p>	<p><b>Article XXII:</b></p> <p>Article XXII gives the trustee a sole discretion to determine that it is no longer advisable or necessary to continue the family trust. The trustee has the power to make the decision to pay over and distribute the entire principal of the family trust to the beneficiaries.</p> <p>Doherty argues that Article XXII is put in place to provide for those instances where trust assets are so limited, that is economically and practical to maintain the trust, however, no such limiting restriction is found in the language of the family trust. If this was the intention of the drafters, such language should have been included in the instrument.</p> <p>According to the plain language of the family trust, the trustee’s discretion is extremely broad. As was stated by the Hearing Officer, “The trustee, in its sole discretion, could just as readily determine that the trust assets had grown too large to administer or, in the alternative, that Doherty’s unforeseeable needs are such that it required the termination of the trust.”</p> <p>Doherty is a lifetime beneficiary as is established by Article II and, per Article XXII, the Trustee has discretion, at any time and for any reason, to pay over the principal to Doherty during her life.</p> <p>The Court noted that these provisions appear to be in direct conflict with Article V.A.’s prohibition against distributing principal to Doherty. Under the traditional trust law, it is true that the court would look to the settlor’s intent to reconcile these provisions but, in this case, the family trust must be analyzed in light of the prevailing public policies in federal and state Medicaid laws.</p>	<p><b>Article XXII:</b></p> <p>At first blush, MassHealth’s conclusion seems a bit odd insofar as trust Art. V.A.2 explicitly provides, as noted, that the trustee may “make no distributions of principle from the Trust, to or on behalf of Muriel. But as MassHealth strongly presses upon us, this clause may not be read in isolation; rather, it must be construed and qualified in light of the trust instrument as a whole. See Harrison v. Marcus, 396 Mass. 424, 429 (1985). Taking this maxim to heart, we observe that trust Art. XXII generally provides that the trustee may, “in its sole discretion” and notwithstanding “anything contained in this Trust Agreement” to the contrary, “pay over and distribute the entire principle of [the] Trust found to the beneficiaries thereof, free of all trusts” so long as the trustees, “in [their] sole judgment,” determine that the “fund created...shall at any time be of a size which...shall make it inadvisable or unnecessary to continue such Trust fund.” Similarly, trust Art. XIV.H gives to the trustee the power to “determine all questions as between income and principal and to credit or charge to income or principal or to apportion between them any receipt or gain...notwithstanding any statute or rule of law for distinguishing income from principal or any determination of the Courts.” [FN5]</p>

## DO NOT RESCUE RIGHT TO USE HOME

The Family Trust also granted Muriel Doherty, as the Donor, the right to occupy the residence known as 15 Chestnut Street, Andover, which can only be sold by the Trustee with express permission. This provision would make the home countable under 130 CMR 520.023(C)(1)(d), which states that the home, or former home of the nursing facility resident or spouse held in an irrevocable trust that is available according to the terms of the trust, is a countable asset.

The Appeals Court ruled: “We take this opportunity to stress that we have no doubt that self-settled irrevocable trusts may, if so structured, so insulate trust assets that those assets would be deemed unavailable to the Settlor.” Guerriero v. Commissioner of the Division of Medical Assistance, 433 Mass. 628, 633 (2001).

### **Recommendations:**

- Payment of income to the Grantor is permissible.
- Prohibit any and all distributions or the use of principal.
- Limit lifetime powers of appointment to a charity (to assure grantor trust status).
- Retain Testamentary Limited Power of Appointment (Appeals Court did not mention this as a factor that it considered in upholding the Superior Court.)