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THE RECORDER

Rebels get seat at backroom budget talks

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SACRAMENTO — In what has become a yearly ritual, Capitol staffers are huddling up again with lawyers, judges and labor groups to figure out how to absorb another big hit to the judiciary budget. This year, however, some new faces have joined the closed-door gatherings.

Capital Accounts

Legislative leaders have invited members of the Alliance of California Judges to join the budget talks, which have been the traditional realm of representatives from the 2,600-member California Judges Association, trial lawyers, defense counsel and employee groups. A recent meeting, though, included alliance Directors Stephen White, presiding judge of Sacramento County, and Kern County Superior Court Judge David Lampe.

"I think it's a recognition that we're very much stakeholders," White said, "and that any body of several hundred judges should be included in discussions about the budget."

The alliance's inclusion suggests a growing respect in some legislative circles for the fledgling judges group, which one Capitol staffer credited with "raising red flags" on "credible issues" within the judiciary. Chief among those issues is the California Court Case Management System, the branch's in-development computer network that the state auditor declared over-budget and poorly managed.

CCMS, and the alliance's opposition to its continued funding, was a topic of discussion at the recent meeting as was the general desire to keep courthouses open despite the cuts, White said. No decisions were made, however, and additional talks are expected.

Asked if the alliance was well-received at the meeting, White said, "Certainly by the legislative representatives."

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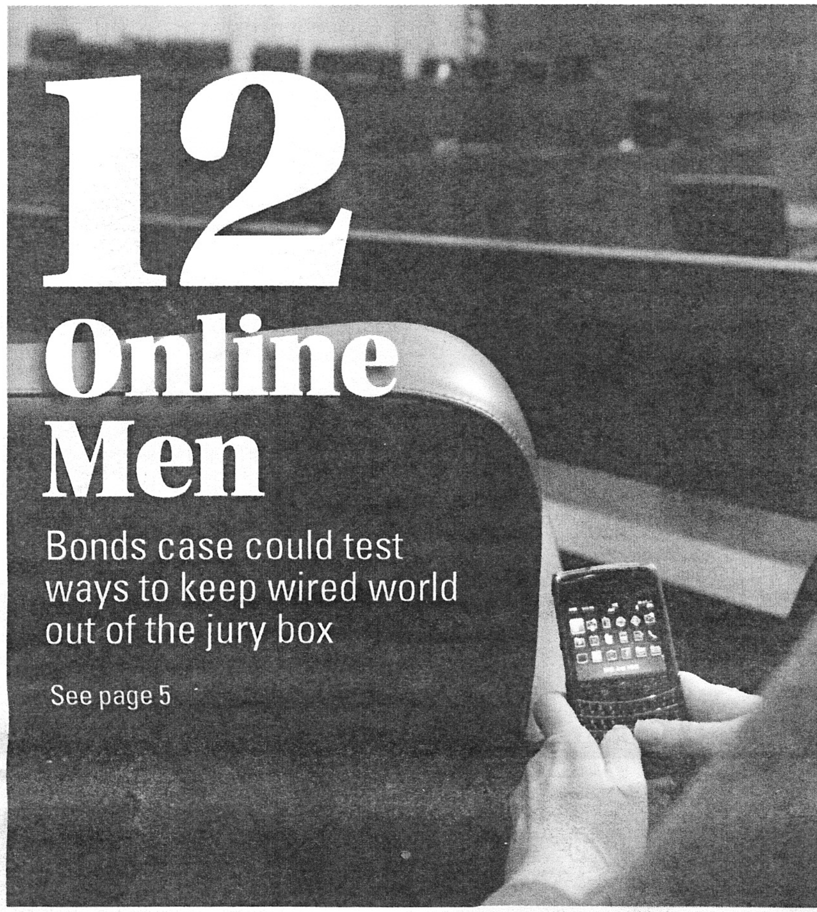

PHOTO ILLUSTRATION BY JASON DOIY

2011: The year of the IPO?

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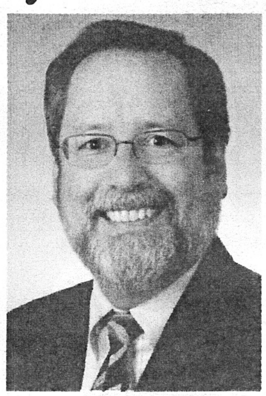
Lawyers in Silicon Valley predict that 2011 could be the busiest year for IPOs since the dot-com bubble burst, if offerings in January and February are any indication.

So far this year, at least seven Bay Area companies have issued or announced plans for an IPO. The most anticipated debut is LinkedIn Corp., which filed to go public on Jan. 27, without disclosing exactly how much money it plans to raise.

"It's a natural outgrowth of market improvements," said DLA Piper M&A partner Peter Astiz, who's also global co-head of the firm's technology sector. "At the end of the day, people are looking for real returns on their investment, and IPOs are the traditional source for a lot of those high-growth opportunities."

The Bay Area isn't the only region seeing a surge in IPO activity this year, thanks to growing stability and confidence in the U.S. stock markets. As of Feb. 11, 23 companies had gone public in the United States so far this year, raising a total of $8 billion, according to Greenwich, Conn.-based Renaissance Capital. That's a 313 percent increase in dollar volume over this time last year, when 13 companies went public and raised $1.9 billion.



GOING PUBLIC: DLA Piper M&A partner Peter Astiz has worked on three IPOs since the beginning of this year. Last year he worked on four total.

The tech sector accounted for seven IPOs nationwide in the last 12 months, according to Renaissance, the most of any industry sector. There were five health care IPOs in the same period.

In Silicon Valley, business lawyers say IPOs are keeping them busier than they have been in years. In the last two weeks, three Bay Area companies advised by Cooley lawyers have held public offerings: Epocrates Inc., which makes drug reference applications for doctors' mobile devices; NeoPhotonics Corp., which makes cir-

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Self-settled pooled trusts

There are ways persons receiving government assistance can shelter additional assets to maintain their eligibility

Thomas E. Beltran

Trusts and Estates

Persons with disabilities receiving cash or other assets — successful litigants in personal injury actions, for example — must take care to shelter the cash or assets received when they are also recipients of needs-tested public benefits such as Supplemental Security Income and Medicaid (known as "Medi-Cal" in California). This is due to a rule, typical of many programs, limiting assets for public benefits recipients to no more than $2,000, exclusive of certain exempt assets such as a car or residence. For a number of reasons, a litigant with disabilities will often elect to shelter the funds in a special needs trust. The successful litigant, establishing a special needs trust with his or her own assets, would be both the grantor (or settlor) and the beneficiary. The resulting special needs trust is referred to as a "first party," "self-settled," or "(d)(4)(A)" special needs trust.

There are two factors which limit access to this resource shelter. First, the person with disabilities must meet the strict Social Security test of disability, and second, the person must be under the age of 65. Therefore, an elderly person residing in a Medi-Cal funded nursing home, who recovers in a suit for nursing home abuse, for example, would ironically, upon receipt of the award, lose her Medi-Cal funding because her assets would exceed the resource limits, and an individual special needs trust would be unavailable due to age. Except for a narrow range of non-penalized transfers, that person would then need to spend down the assets to below the $2,000 asset limit before Medicaid long-term care would resume. A remedy is a self-settled (or first-party) pooled special needs trust.

The federal authority governing the establishment of first-party special needs trusts is found at §1917(d)(4)(A) of the Social Security Act, known as the Omnibus Budget Reconciliation Act of 1993 (OBRA '93), codified at 42 U.S.C. 1396p(a)-(e). Post OBRA '93, an individual disposing of resources to become eligible for Medicaid benefits may be penalized, depending upon how the disposition of assets is characterized.

TWO TYPES OF TRUSTS

Within the class of first-party trusts that can be established under OBRA '93, there are two subclasses available in California — individual trusts and pooled trusts, similar to an attorney's client trust account. Individual first-party trusts, most likely numbering in the thousands in California, are far more common than pooled trusts, of which there are approximately six.

With the exception of two very significant distinctions concerning trust establishment and a third, relating to termination, individual and pooled special-needs trusts are otherwise similar and accomplish the same purpose — to shelter assets that otherwise exceed the public benefits resource limits, allowing future use by the person with a disability to meet his or her unmet need.

In establishing a (d)(4)(A) trust, the public benefits recipient cannot establish the trust himself. It must instead be established by a "parent, grandparent, legal guardian of the individual, or a court." (§1396p(d)(4)(A)) By contrast, a (d)(4)(C) trust can be established by the public benefits recipient, in addition to those persons/entities. (§1396p(d)(4)(C)(iii)) Even more significant, however, is the absolute bar to establishment of a (d)(4)(A) trust by a person over the age of 65. By contrast, the statutory language of section (d)(4)(C) contains no such restriction. Finally, upon termination, the remaining assets in a (d)(4)(A), up to the amount equal to the total medical assistance paid by the state plan, are returned to the state. The remaining assets in a (d)(4)(C) trust can be retained by the nonprofit entity, with the state recovering the remainder, if any, up to the amount equal to the total medical assistance paid by the state plan.

FEDERAL MEDICAID AGENCY INCORRECTLY INFERS AGE LIMIT

The Centers for Medicare & Medicaid Services (CMS) — the agency that oversees the Medicaid and Medicare programs — released a Massachusetts State Agency Regional Bulletin, dated May 12, 2008, stating that "a pooled trust may be established for beneficiaries of any age." This statement is significant in that some commentators have suggested either that Congress mistakenly omitted the reference to age in section (d)(4)(C), or an alternative interpretation, that under the SSI program, an individual, upon reaching age 65, is no longer considered to be disabled because disability benefits terminate and the individual then becomes eligible for old age benefits. The bulletin goes on to advise that "only trusts established for a disabled individual age 64 or younger are exempt from application of the transfer of assets penalty provisions (see §1917(c)(2)(B)(iv) of the act)." In other words, the position taken in the bulletin is that the establishment of a (d)(4)(C) trust by a person over the age of 65 will not be penalized unless that person seeks long-term care.

Fortunately, the bulletin is not controlling law; even regulations, promulgated in accordance with the Administrative Procedures Act, are not given deference when they are inconsistent with congressional intent and "arbitrary, capricious, or manifestly contrary to the statute." *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984). Even if the bulletin had the force of a regulation, the position taken by CMS conflicts with the plain language of the statute. Unlike regulations, however, the CMS interpretation as stated in the bulletin has not undergone the rigors of the Administrative Procedures Act and would not be subject to the deference accorded regulations. *Christensen v. Harris County*, 529 U.S. 576 (2000).

The opinion presented in the CMS bulletin rests upon the erroneous assumption that when a person establishes a trust with the funds, he or she gives up ownership of those funds such that the establishment of a first-party special needs trust can be penalized as a "transfer for less than fair market value." This assumption fails to take into account the internal construction of the statute, as well as the basic Social Security Act principle that a grantor of a first-party trust, upon funding the trust, retains equitable ownership of the trust assets.

ASSETS CONTINUE TO BE THE SETTLOR'S

The general rule concerning irrevocable trusts, subject to exceptions found in Subsection (d)(4), is that assets placed in a self-settled trust continue to be assets countable or attributable to the individual by virtue of his equitable ownership. As long as the assets are used (or could be used) for the benefit of the grantor/beneficiary, he continues to have an equitable interest in the assets. This is what distinguishes a transfer of assets (subsection (c)), from the establishment of a trust (subsection (d)).

The principal of equitable ownership is demonstrated under social security law, in the context of determining in-kind support. If an SSI recipient resides in a home without paying rent, the rental value is considered in-kind income, which reduces the monthly cash payment. But the Social Security Administration's Program Operations Manual System (POMS) states that if the SSI recipient resides rent-free in a home owned by his or her special needs trust, he or she is deemed to be the owner, on the basis of his equitable ownership, and no in-kind support is attributed to his rent-free use of the home.

It is clear from the foregoing discussion that there is no subsection (c) transfer penalty for placing assets into a self-settled trust, unless assets from the trust are then transferred for "any other purpose" than the benefit of "the individual," or the assets cannot be distributed for the benefit of the individual "under any circumstances." Therefore, it is incorrect to apply the subsection (c) limitation for a transfer of assets to a trust, including a trust established under subsection (d)(4), when the trust is self-settled and the trust assets can be expended, but only for the benefit of the beneficiary.

When an individual establishes a special-needs trust with his own assets, and the trust is for his own benefit, the transaction is not a transfer for purposes of long-term Medicaid (which is governed by subsection (c)), but an entirely different transaction — it is the establishment of a trust, which is governed by subsection (d). This is because the settlor/beneficiary is not divested of ownership, which is required for the transaction to be a transfer, but instead retains equitable ownership of the trust assets.

Therefore, the statement in the bulletin that "[w]hen a person places funds in a trust, the person gives up ownership of those funds.... [s]ince the individual generally does not receive anything of comparable value in return," is incorrect except in a very specific context. That specific context occurs in subsection (d), where the individual places his or her assets into a trust for his or her own benefit, and then such assets are distributed in a manner that does not benefit the individual/beneficiary, or under the terms of the trust cannot be distributed under any circumstances for the benefit of the grantor/beneficiary. In that case, the transaction is partially recharacterized as a below-market transfer, which is then penalized under subsection (c), to the extent the trust assets can be distributed to someone other than the self-settlor, or cannot be distributed at all.

CONCLUSION

The construction advanced by the CMS in its regional bulletin is erroneous because it fails to take into account the difference between the establishment of a trust with one's own assets, which is governed by subsection (d), and a transfer of assets, which is governed by subsection (c). CMS however, still regards its interpretation as authoritative.

Elders with disabilities can place their assets in a self-settled, pooled, special-needs trusts without the imposition of the Medicaid transfer penalties. While the statutory construction is clear, practitioners should take certain precautions:

First, obtain court approval for the establishment of the trust (or self-settled trust for a person aged 65 or over). Court establishment provides a forum where any objections, or questions about construction raised by the Department of Health Care Services, can be resolved before what will be an irrevocable trust is established.

Second, although California's Department of Health Care Services has unofficially stated that it will not penalize the establishment of a pooled trust by a person over the age of 65, for purposes of long-term care, one should, in giving notice to the Department of Health Care Services, put a synopsis of the argument in the attorney-drafted notice. One benefit of assuring that the department is well aware of the transaction and the basis therefore is to assure that collateral or administrative estoppel attaches.

Third, care should be taken when the pooled trust is established for a person aged 65 and over who receives or is anticipated to again receive SSI because this is still uncharted territory. The distinction between a transfer of assets and establishment of a trust under the SSI rules is not quite as clear as in the Medicaid statute. Notice should be given to the Social Security Administration at the earliest opportunity to allow resolution. In fact, it may be wise to begin working on the SSI issue as soon as it is probable that a pooled trust will be needed. This is because it is unclear what position the administration will take. POMS states that a transfer of assets into a pooled special needs trust by a person over the age of 65 "may result in a transfer penalty." Therefore, one must exercise care in properly setting up the SSI case. When the evidence is that the elderly grantor cannot reasonably live in a setting that is less restrictive than a nursing-home, such notice may not be necessary, because SSI would go into suspense when a person resides in a Medicaid-funded facility, and after 12 months Social Security Administration benefits terminate.

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