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October 15, 2018

The Honorable Tani Cantil-Sakauye,
Chief Justice, and Associate Justices
Supreme Court of California
350 McAllister Street
San Francisco, CA 94102-4797

Re: *Scott v. McDonald* (August 22, 2018)
Fourth District. E06272

**REQUEST FOR DEPUBLICATION**

Honorable Justices:

We write on behalf of the American College of Trust and Estates Counsel (ACTEC) to request depublication of the *McDonald* case pursuant to California Rules of Court, Rule 8.1125.

In *McDonald*, the Fourth District Court of Appeal, Division Two, upheld the imposition of a $92,036.75 surcharge on a trustee of a special needs trust (SNT). While the facts of the case suggest the surcharge was appropriate, the Court of Appeal's decision was based on a conclusion that the terms of the trust did not permit the trustee to use trust funds for the support of the beneficiary. This conclusion is inconsistent with the terms of the trust and with the provisions of the Social Security Act that allow persons with disabilities to have money held in trust for them. If this ruling becomes precedent, beneficiaries of SNTs may be denied legitimate benefits from their trusts.

Any application of the holding in this case to the administration of SNTs is likely to cause immediate, serious, and irreparable harm to thousands of Californians (and citizens of other states should the ruling be adopted by other courts) with disabilities by:

1. Creating a citable opinion contrary to longstanding federal and state law and policy on the proper use of SNT funds;
2. Placing limitations on the future use of SNT's for persons with disabilities, contrary to the stated intent behind Congress' authorization of SNTs; and

3. Jeopardizing both SNT drafters and SNT trustees who have been appropriately drafting and administering SNT's by creating confusion as to the fundamental legal standards they have been using for decades of planning and administration.

**ACTEC's Interest as Amicus Curiae**

ACTEC is a nonprofit organization of more than 2,500 trust and estate lawyers and law professors from throughout the United States, Canada, Central and South America, Europe and Asia. Approximately 165 Fellows are California attorneys. Fellows of ACTEC are skilled and experienced in trust and estate law and are elected by their peers on the basis of their professional reputation, quality of their work, and their substantial pro bono contributions to the practice and the public, including lecturing, writing, teaching, and drafting court rules and legislation. ACTEC is dedicated to enhancing trust and estate law and practice through research, education, technical advice to governments, and, on rare occasions, assisting courts in understanding this discrete area of the law.

Established in Los Angeles in 1949, ACTEC's office is now located in Washington D.C. and is governed by 39 Fellows who serve on its Board of Regents, six of whom are the officers of ACTEC. Much of the work done by ACTEC is performed by committees including the Amicus Review Committee. The Amicus Committee and the officers of ACTEC voted unanimously to approve ACTEC's submission of this request for depublication. The Amicus Committee consulted with ACTEC's Elder Law Committee in reaching its decision.

In this case, ACTEC believes that it can assist the Court in understanding the serious implications to both California and sister-state trust law of allowing this decision to stand as precedent for the administration of SNTs. ACTEC and its committees focus, among other things, on discussing and making available to its members and to other attorneys best practices regarding drafting and implementation of trusts, including SNTs. In so doing, ACTEC and its attorneys rely upon direction provided by appropriate regulatory agencies, in this case, the Social Security Administration (SSA),[1] case law interpreting the appropriate regulations and case law interpreting trusts in general. In the case of SNTs, where the impact of misinterpreting the regulations is the potential of clients being disqualified from government benefits, strict adherence to regulations and prior interpretations of those regulations from the governing body leads to creation of trusts with specific and well-accepted language that is known not to disqualify beneficiaries. The use of specific and well-accepted language is thus a best practice in trust drafting in this particular area. The appellate court's ruling in this case would, by applying incorrect

[1] There were not then, and are not now, any specific federal regulations concerning SNTs. The main federal guidelines for SNTs are found in the SSA's Program Operations Manual System (POMS). The courts generally defer to the POMS as reflective of the appropriate interpretation of the rules for receipt of disability income the SSA. (*See, e.g. Draper v. Colvin* (2015)779 F.3d 556 at 561.

standards to the interpretation of well-accepted language, potentially necessitate modification of virtually every SNT.

**Depublication Is Necessary Because the Court of Appeal's Decision Interpreted the SNT Document in a Manner Contrary to the Stated Intent of Congress in Authorizing SNTs and Contrary to Longstanding Principles of Trust Interpretation**

**SNT Background**

Title XVI of the Social Security Act provides, "[e]very aged, blind, or disabled individual who is determined ... to be eligible on the basis of his income and resources shall ... be paid benefits by the Commissioner of Social Security." 42 U.S.C. § 1381a. However, when such an unmarried individual's personal resources exceed $2,000, he or she loses eligibility for Supplemental Security Income (SSI) benefits. 42 U.S.C. § 1382(a)(3)(B). Certain assets are exempt from being counted against this $2,000 limit, however, including special-needs trusts under § 1396p(d)(4)(A). 42 U.S.C. § 1382b(e)(5). *See, Draper v. Colvin* (2015)779 F.3d 556 at 559. In California in 2018, the maximum income payable to a person entitled to SSI is $910.72 per month.

In light of the significant income and asset limitations for SSI eligibility, Congress authorized the use of SNTs in 1993 at 42 U.S.C. §1396p(d)(4). SNTs allow a person with disabilities to enjoy those extra things that enhance the quality of life without causing the payment for those items to jeopardize the person's eligibility for public benefits. An SNT allows a person with a disability to have money held in trust for him or her that does not count against his or her $2,000 resource limitation for SSI and Medi-Cal. California has adopted the federal rules authorizing SNTs in California. See, 22 Cal Code Regs §§50489–50489.9. SNTs may be either self-settled (as is the case in *McDonald*) or settled by a third party.

**The Appellate Court's Improper Interpretation**

The *McDonald* court purported to apply California trust law to the interpretation of the SNT at issue. It strictly construed the Trustee's ability to use trust funds, limiting the Trustee to expenditures "made necessary by the beneficiary's disabilities." At the same time, it expansively construed the meaning of the language "this is not a trust for the support of the beneficiary" by concluding that this provision prohibited payments made in the discretion of the trustee that contributed to the beneficiary's support. Both interpretations are unsupported by California or general trust law and contradict the intent of the statute authorizing SNTs.

The basic rules of trust interpretation in California are set forth in Probate Code §§21101–21140. These rules are similar to the rules common throughout the United States for trust interpretation. Of primary import is the rule that the trust should be

interpreted according to the intent of the trustor. Prob. C. §21102; *Estate of Duke* (2015) 61 Cal.4th 871, at 884. In determining that intent the words of the instrument should be interpreted so as to give every expression some effect and construed such that the words form a consistent whole. Prob. Code §21120 and 21120. The *McDonald* court failed to apply these basic interpretation rules, never addressing the issue of the trustor's intent and basing its ruling on only limited language rather than on the trust as a whole. Moreover, the court failed to address at all the federal regulations governing SNTs.

The *McDonald* case cited to the intent language of the trust as follows:

> "C. The intent and purpose of this trust is to provide a discretionary, spendthrift trust, to supplement public resources and benefits when such resources and benefits are unavailable or insufficient to provide for the Special Needs of the Beneficiary. As used in this instrument, the term 'Special Needs' means the requisites for maintaining the Beneficiary's good health, safety, and welfare when, in the discretion of the Trustee, such requisites are not being provided by any public agency, office, or department of the State of California, or of any other state, or of the United States of America. The funds of the trust may be used as an emergency or backup fund secondary to public resources. Special Needs include without limitation special equipment, programs of training, education and habilitation, travel needs, and recreation, which are related to and made reasonably necessary by this Beneficiary's disabilities. This is not a trust for the support of the Beneficiary. All payments made under this Trust must be reasonably necessary in providing for this Beneficiary's special needs, as defined herein."

Despite having quoted the entire paragraph, in reaching its conclusions, the appellate court focused solely on the last few lines, in particular the words "which are related to and made reasonably necessary by this Beneficiary's disabilities" and "[t]his is not a trust for the support of the Beneficiary." The court ignored the fact that the first phrase was included in a sentence defining "special needs" **without limitation**. The Court further ignored the prefatory language of the section about requisites for "maintaining the Beneficiary's good health, safety, and welfare" and the overall intent to "supplement" public needs benefits. It seems apparent from the facts of the case that the Court was intent on upholding the surcharge to the trustee. Although ACTEC does not disagree with the ultimate finding as to surcharge, unfortunately, in focusing on the trustee's wrongdoing without properly applying the usual standards for trust interpretation, the Court created the potential for chaos in the drafting and administration of SNTs.

Similarly, the Court of Appeal clearly misunderstood the use of the term "support trust." The term "support trust" is generally understood to refer to a trust the terms of which require the trustee to provide payments for its beneficiary's support. As referenced

above, in addition to the monthly income limitations to qualify for assistance, there is under the federal law a prohibition on a beneficiary having countable assets beyond the $2,000 limit. Trusts that would require the trustee to "support" the beneficiary or to otherwise provide funds on any but a discretionary basis create a disqualifying situation for the beneficiary by giving the beneficiary "countable" resources above the allowable limit. (See 42 U.S.C. §1382b(e)(3)(A), 20 C.F.R. §416.1201(a)(1); POMS SI 01120.200(D)(2)). Therefore, there is a good reason that an SNT would never be a support trust and, in fact, would contain language clarifying that it is **not** a support trust. Every properly drafted SNT is a discretionary, spendthrift trust, and is not a "support trust." (For a detailed discussion of the differences among such trusts, see Restatement Trusts 2d, §§152, 154 and 155.) The Court of Appeal apparently misunderstood this basic aspect of SNTs, interpreting the language in question to mean that the trustee could not provide to the beneficiary anything that could be considered "support" rather than interpreting the language to clarify that the trustee was not obligated to provide support. This, of course, flies in the face of established law concerning SNTs.

The court's interpretation here is particularly troubling as there is no regulatory provision that prevents the application of SNT funds to support of a beneficiary or even the use of funds for third parties who are providing assistance to the beneficiary. (See, e.g. SSA POMS SI 01120.200(E)(1)(c): Disbursements that do not count as income may include those made for educational expenses, therapy, transportation, professional fees, medical services not covered by Medicaid, phone bills, recreation, and entertainment. This list is illustrative and does not limit the types of distributions that a trust may permit.) As there is no regulatory prohibition on what may be paid for, careful SNT drafters make sure not to impose additional restrictions. It would make no sense for the settlor of such a trust to limit how the trust could benefit the beneficiary so long as those benefits do not run afoul of the federal regulations. The whole purpose of SNTs is to allow a beneficiary to have a more normal life despite his or her disabilities and the severe restrictions imposed by the income limitations of disability benefits.

**The Impact**

Unfortunately, this is not a situation in which the appellate court's interpretation of language in a single trust will impact only the case in front of the court. The language used in the trust in question is not unique or poorly drafted language. It is remarkably similar to language used in countless SNTs throughout California and other states. This interpretation will immediately call into question decisions that have been made by Trustees for over 25 years based upon the plain reading of the language contained in an SNT. The language of this trust matches other SNTs throughout the country because SNTs must be strictly drafted so as to avoid running afoul of the rules concerning inclusion of income for a disabled beneficiary. Careful attorneys drafting SNTs look to the regulations provided by the SSA through the POMS and interpretations of those regulations in case law to ascertain the proper language to use in their trusts. As a result,

SNTs drafted by careful and well-respected attorneys, will contain virtually, if not completely, identical language. As a result, the appellate court's application of incorrect standards to the interpretation of this trust instrument will call into question the way in which substantial numbers of trustees have interpreted the language in many other trust instruments drafted since the original authorization of SNTs by Congress. This single case will both put at risk trustees who have relied upon earlier interpretations of this language to make distributions and create chaos in the planning of SNTs. Attorneys will now need to draft new language to avoid the potential of another court relying upon this court's interpretation with the attendant risk that the new language will **not** satisfy the SSA's guidelines, thus putting beneficiaries at risk of losing their government benefits.

For more than two decades, trustees of SNTs have been making payments of the sort made in the *McDonald* case for the benefit of disabled beneficiaries of those SNTs. Over that same period of time, drafters of SNTs have worked to ensure that the language being used in those trusts complies with the requirements of federal law so as not to create disqualifying events for those beneficiaries. If the *McDonald* case stands as published law, with its flawed and inaccurate interpretation of this particular trust and of SNT rules in general, it will create chaos in the drafting and administration of these trusts. As a result ACTEC strongly urges this court to depublish *McDonald*.

Sincerely,

Charles D. Fox IV
ACTEC President, 2018-19

Margaret G. Lodise
Chair, ACTEC Amicus Review Committee

## PROOF OF SERVICE BY U.S. MAIL

STATE OF CALIFORNIA
COUNTY OF LOS ANGELES

I am employed in the County of Los Angles, State of California. I am over the age of 18 and not a party to the within action; my business address is 350 S. Grand Avenue, Suite 3500, Los Angeles, California 90071-3475.

On **October 15, 2018**, I served the foregoing document described as **LETTER RE REQUEST FOR DEPUBLICATION** on the parties by placing true copy(ies) thereof in a sealed envelope(s) addressed as follows:

***SEE SERVICE LIST***

__X__ I deposited each envelope in the mail at Los Angeles, California. Each envelope was mailed with postage thereon fully prepaid.

__X__ As follows: I am 'readily familiar' with the firm's practice of collection and processing correspondence for mailing. Under that practice it would be deposited with the U.S. postal service on that same day with postage thereon fully prepaid at Los Angeles, California in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after date of deposit for mailing in affidavit.

Executed on **October 15, 2018**, at Los Angeles, California.

____ (State) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

Michisha Jiles

Signature

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