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ELDER LAW BASICS:

CLIENT CONCERNS, BENEFITS QUALIFICATION AND ESTATE RECOVERY AVOIDANCE

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A. CLIENT CONSIDERATIONS

While it may seem obvious, a critical concern is whether your client is competent. However, making this determination can be quite difficult, especially given the limited time with a client. Therefore, it is often helpful to engage the client in longer conversations such that deficiencies may reveal themselves over the course of the conversation (e.g., client begins to repeat himself, or it becomes clear that the client's impressively detailed story is actually one they often tell from long ago while being quite unclear as to his or her present circumstances). Thereafter, it is advisable to make notes as to conversations had with the client, to which you can refer during a current representation, and upon which you can rely if capacity is called into question at a later date. Quick cognitive tests such as the clock test or other cognitive assessment rubrics also provide a feel for capacity; however, more definitive assessments such as the MMSE (Mini Mental State Examination) and MoCA (Montreal Cognitive Assessment) are best left to a physician to interpret. If a client shows signs of diminishing capacity such that it is too difficult to make a determination, it may be advisable to recommend the client visit the doctor to obtain a medical opinion. Capacity can be a tricky assessment, but documentation and attention to detail can help both you and your client in the long run.

Unfortunately, when working with elderly clients, we also must be alert to potential elder exploitation. While you cannot form a protective barrier around your client, you can arm them with useful tips to help them protect themselves from financial abuse. For example, encourage clients to discuss any changes in investment strategy or new products with a trusted advisor (attorney, CPA, financial planner, etc.) and not to be afraid to ask for a second opinion. A good advisor will be aware that older individuals should avoid products that are not age/risk appropriate or have early withdrawal fees since fixed income clients may need immediate access to the money. Good counseling for elderly clients can also include advising them on safe banking practices such as:

1. Maintaining custody of credit cards and checkbooks in a secure location where nosy family members or guests cannot access them;
2. Reconciling bank and credit card statements monthly. Exercising reasonable promptness in examining statements and alerting the bank to unauthorized activity increases the likelihood that the bank will replenish the account;
3. Considering an arrangement with the bank whereby checking accounts have low balances to meet basic monthly needs; and
4. If online banking is used, frequently changing passwords.

In order to ensure that your clients' needs are being served on multiple levels, attorneys often ask whether clients have their wills, trusts and powers of attorney in place. From an elder law perspective, you may also consider asking the following related questions:

1. Is your client or a potential beneficiary an individual with special needs? Is the client or beneficiary receiving benefits, or may need to receive benefits, such as Medicaid, Special Assistance, SSI or SSDI? Asking these questions will enable the attorney to ensure that such an individual receives funds in a way that does not disqualify them from public assistance now or in the future.

2. As a follow-up to the first question, determine whether a special needs trust has been or needs to be established.

3. If the client or beneficiary does have special needs, determine whether a guardianship has been or needs to be established.

4. Is your client being paid under a caregiver agreement? These are common and useful tools in benefits planning; however, this income needs to be reported on the caregiver's tax return, which the caregiver may not realize.

B. BASIC MEDICAID AND SPECIAL ASSISTANCE CONCERNS

1. Basic Qualification Rules for Medicaid and Special Assistance.

Just like all tissues are not Kleenex, not all long term care benefits are provided by Medicaid, even though we often hear these proper terms used as shorthand. Medicaid provides benefits for those in skilled nursing facilities. The qualification for Medicaid is largely asset-driven, although the applicant's income is considered. For example, a recipient can only have $2,000 in all cash or cash equivalent assets, a residence up to $536,000 value, one vehicle, personal effects, etc.

Conversely, Special Assistance benefits are available for those in assisted living facilities and for some in-home care. While Special Assistance qualification involves similar asset requirements to Medicaid, it has much stricter income limits: $1,247.50/month or $1,580.50/month for Alzheimer's or qualified memory units. If the applicant receives even $1/month more than the limit, the applicant will be summarily denied. (Note: asset and income limits are as of the date of this manuscript.)

2. Basic Planning Goals of Medicaid and Special Assistance Applicants

While individuals seeking assistance for long term care benefits have myriad needs and goals, two goals are paramount from a planning perspective: (1) avoidance of transfer sanctions and (2) avoidance of estate recovery.

First, the applicant wants to avoid transfer sanctions as much as possible. Many applicants are over the eligibility limits when they first consider applying for benefits. Therefore, the applicant needs to reduce his or her countable assets to meet the eligibility limits in a manner that does not otherwise disqualify or delay them from receiving Medicaid or Special Assistance benefits.

For Medicaid qualification, the applicant is subject to a 5-year lookback period under Medicaid transfer rules. If a sanctionable transfer (i.e. a gift or a transfer for less than market value that does not fall within transfer exceptions) is made within the five years prior to the date the applicant is otherwise qualified for Medicaid, the value of the transfer will be divided by $6,300. The resulting figure equals the number of months from the month that the applicant was otherwise qualified (i.e. met all the eligibility requirements), during which period the Medicaid applicant will not receive Medicaid. In other words, the sanction period acts as a waiting period for the applicant until Medicaid will begin to cover the cost of care. From a practical perspective, during this sanction period the applicant will somehow have to private pay for his or her care until Medicaid begins.

Under Special Assistance transfer rules, the applicant is subject to a 3-year lookback period. If a sanctionable transfer is made, the value of the transfer will be divided by $2,000. The resulting figure is the number of months beginning the month after the month of the sanctionable transfer during which the Special Assistance applicant cannot receive Special Assistance, meaning the penalty period begins the month after the transfer. Please note that this period runs differently than Medicaid since the sanction period runs from the time of transfer, not from the time that the applicant is "otherwise eligible." However, this sanction period can still create a financial hardship for the applicant, which he or she certainly wants to avoid as much as possible.

The applicant's second major goal is to avoid estate recovery. Upon the death of a benefit recipient, the government will file a claim against the benefit recipient's estate, through which the government seeks to be repaid for benefits provided during the recipient's lifetime. Therefore, while trying to reduce the applicant's assets for qualification purposes, the applicant/recipient also wants to ensure that any assets that the applicant is allowed to keep are not subject to estate recovery upon the applicant's death. Typically, the only asset of value remaining in the recipient's estate is the real property an applicant/recipient was allowed to keep even though they were able to qualify for benefits. Without planning, that real property is likely subject to estate recovery rather than being available for distribution to heirs.

3. Spend Down Strategies and Pitfalls

Given the prior discussion of transfer sanction period, as an applicant is spending down his or her assets to fall under the asset limits for receipt of benefits, an applicant clearly needs to be mindful of how and where those assets are moved. During spenddown, an applicant may be inclined to make a large transfer or gift to a spouse or other family member. Proceed with caution! Many of these transfers will create a sanction period during which the otherwise impoverished applicant will not receive benefits. Moreover, some transfers may be safe under certain circumstances, but create issues under others. For example, although transfers to a spouse when qualifying for Medicaid generally do not trigger sanctions, the spouse may end up with more assets in his or her name than allowed under the Community Spouse Resource Allowance (CSRA), meaning that the spouse then needs to spend down his or her assets. As such, rather than simply making a gift, the applicant may want to take advantage of benefit-friendly vehicles such as Medicaid qualified annuities, properly structured promissory notes, or trusts, all as part of a comprehensive plan.

Another option is to transfer assets into certain types of irrevocable trusts. Assets held in these properly structured trusts are not counted against the applicant/recipient's asset limits. These assets will also not be part of the applicant/recipient's probate estate; therefore, Medicaid may not reach these assets to satisfy their claim upon the applicant/recipient's death. However, such transfers typically do have transfer sanction implications. One exception, as further discussed below, is that transfers to certain sole benefit or special needs trusts may not trigger transfer sanctions. Please note that certain of these special needs trusts may contain payback provisions that <u>do</u> make them subject to estate recovery. Clients should consult an attorney to ensure transfers and trusts are properly structured for that client's circumstances.

Clients should also be mindful that gift and estate tax friendly tools are often not friendly to those trying to qualify for benefits. For example, although making an annual exclusion gift of $15,000 does not trigger a gift tax event, it likely triggers a sanction period. Similarly, while a qualified disclaimer is a good tax avoidance tool, waiver or disclaimer of a right to receive an inheritance will likely be deemed a transfer subject to penalty.

Further, you want to ensure that the client receives advice regarding maintaining sufficient assets to cover their living and health care expenses during the pendency of the qualification process, which often takes several weeks or months, or during a sanction period. These rules are far more nuanced than this presentation reaches. However, what should be clear is that when a client mentions making gifts or transfers for benefit qualification, you likely want to advise them to wait until they can seek counsel from an attorney who understands the qualification rules.

C. SPECIAL NEEDS TRUSTS

1. Generally.

Special needs trusts are incredibly beneficial for individuals who are receiving or who may receive governmental benefits under means-tested programs (e.g., Medicaid and SSI). These irrevocable trusts may allow them to receive assets in such a way that does not disrupt those benefits. The terms of these trusts, timing and means of funding the trusts, the nature of the trust assets, and the individual's needs all must be considered when establishing the trust. These details are best addressed with an attorney who is familiar with special needs trusts during a conversation that is specifically focused on a client's particular circumstances. However, some general considerations when determining whether a client may be interested in setting up such a trust are as follows:

a. Does your client want to pass assets upon his or death to an individual who is, or may be, receiving benefits in such a way that will not disqualify the individual from receiving those benefits? While we often focus on spouses and children, be mindful that a contingent beneficiary, such as a grandchild, may be receiving means-tested benefits and an outright distribution could jeopardize those benefits. Special needs trusts can be a great way to provide for that beneficiary.

b. Does your client, his or her family members or friends want to direct assets during their lifetimes or upon their deaths to an individual who is, or may be, receiving benefits? A stand-alone third party special needs trust may be created into which multiple individuals can direct such assets.

c. Does your client have beneficiary-designated assets (e.g., IRAs, 401(k)s, life insurance, annuities) that are payable to an individual who is, or may be, receiving benefits? These accounts and policies will pay out directly to the named beneficiary, regardless of the terms of a will or existence of a trust, UNLESS the client directs those assets to be distributed to the trust instead. Once a trust is established, this is an easy designation to make.

d. Does your client want to establish who is managing, distributing, and receiving these assets? When your client creates a trust, the client may control who serves as trustee and alternate trustee, as well as who receives any remaining assets upon the death of the trust beneficiary. Please note, however, that in the case of a self-settled trust (trust established with the benefit-recipient's own assets), the

Department of Health and Human Services must be the primary residuary beneficiary.

e. Has a disabled individual received an inheritance, social security backpay, or other infusion of assets that may disqualify the individual from receiving benefits if not quickly handled?

2. Certain Types of Special Needs Trusts

a. Self-Settled Trusts 42 U.S.C. § 1396p(d)(4)(A)

Self-settled trusts allow for the individual seeking benefits to place his or her own assets into an irrevocable trust that is disregarded as a countable asset. In addition, the actual transfer of the assets into a properly structured self-settled trust is a non-sanctionable transfer for purposes of Medicaid and Special Assistance lookback periods. Once placed in the trust, the assets must be unavailable to the beneficiary's control, but the trustee will then use the assets for the exclusive benefit of the beneficiary. In order to qualify, these trusts must meet certain requirements, including:

i. The trust must be established through the actions of the individual, parent, grandparent, legal guardian or court;
ii. The trust must be solely for the benefit of the disabled individual under age 65; and
iii. The trust must provide that upon the death of the disabled individual, the Division of Medical Assistance for the North Carolina Department of Health and Human Services and any similar department in other states furnishing medical assistance shall be repaid prior to making repayment to any other assistance programs to the extent that such payment may be required (hence why these are often referred to as "payback trusts.")

Notably, prior to 2016, a glaring omission from the list of those who could establish a self-settled special needs trust was the individual himself or herself. This created the frustrating situation of having a competent, but disabled, individual without a parent or grandparent, who could not create his or her own trust. The Special Needs Fairness Act addressed this situation, such that the term “the individual” was added to 42 U.S.C. 1396p(d)(4)(A), enabling a benefits recipient to create a self-settled special needs trust without further legal obstacles.

Clearly, these self-settled trusts are extremely helpful in achieving the two major goals in benefits planning of meeting asset qualifications and avoiding sanctions; however, in order to ensure they achieve these goals, it is critical that these trusts are properly structured by an attorney who understands the further requirements and nuances of these trusts, especially regarding allowable distributions. It is also important to note that the compromise for the client is that while his or her own assets can be protected by these trusts, the primary remainder beneficiary must be the State of North Carolina.

Additionally, the situations underlying the need for a self-settled special needs trust are often time-sensitive. Typically, a benefits recipient has come into an unexpected inheritance, life insurance or retirement distribution, or other funds that will push him or her over the reserve limit of $2,000. If not handled immediately, these funds could result in swift disqualification from receiving benefits. The process for establishing a self-settled special needs trust includes gaining approval from HMS and the court, which requires precious time. Therefore, making contact with an attorney who can readily assist with this process is highly advantageous to the client.

b. Third-Party Trusts

Just as the term indicates, these irrevocable trusts are funded by the assets of individuals other than the disabled individual, or his or her spouse. Third-party trusts are a good tool when family or friends want to provide for a disabled individual while ensuring that those assets do not inadvertently disqualify the individual from benefits. Assets can be placed into the trust through lifetime gifts, and the trust can be named as a beneficiary under a will or trust.

In order to ensure that these trust assets are deemed non-countable, they must be “unavailable” to the beneficiary. Assets will be deemed available if the beneficiary has the right to:

i. Revoke or terminate the trust and use the assets to meet his or her food and shelter needs;
ii. Direct the use of trust principal for his or her support and maintenance; or
iii. Assets or sell his or her beneficial interest absent a valid spendthrift clause.

A common error is including an ascertainable, or HEMS, standard for distributions from the trust. While such a standard is advantageous from a tax planning standpoint, it is fatal to a special needs trust. Again, concepts that are advantageous for good tax planning can conflict with elder law goals, making it important to advise clients to consult an attorney well-versed in elder law matters.

c. Testamentary Trusts

Another option is to create a special needs trust within a will or trust, the requirements of which are akin to a stand-alone third-party special needs trust. Clearly, this trust will only arise upon death; however, it does allow for provision of assets to a disabled beneficiary without disqualification from benefits. This is also a good option for a spouse of an elderly disabled beneficiary, as he or she will likely not be able to create an effective third-party special needs trust for his or her spouse.

d. Sole Benefit Trusts

Careful reading of the Social Security Act has given rise to the creation of what have been deemed “Sole Benefit Trusts.” The SSA specifically allows for transfers to certain trusts benefiting either a grantor’s blind or disabled child of any age, or another disabled individual under age 65, which trusts are required to be “solely for the benefit of” the beneficiary. Akin to D4 trusts, the transfers into the trusts do not trigger transfer sanctions and the assets in the trust are non-countable.

In order to be deemed "solely for the benefit" of a spouse, blind or disabled child, or a disabled individual, the transfer must be arranged in such a way that no individual or entity except the spouse, blind or disabled child, or disabled individual can benefit from the assets transferred in any way, whether at the time of the transfer or at any time in the future. Similarly, a trust is considered to be established for the sole benefit of a spouse, blind or disabled child, or disabled individual if the trust benefits no one but the individual, whether at the time the trust is established or any time in the future.

The interpretation of "any time in the future" has led to a further understanding that such a trust must either be a D4 trust, or a trust that contains an actuarially sound distribution standard. In order to be actuarially sound, this trust must include a distribution standard that will ensure complete distribution of the trust within the beneficiary's anticipated life expectancy, pursuant to the tables provided in Transmittal 64.

Why would someone choose to fund a sole benefit trust instead of a third-party trust? If the grantor of the trust is needing to qualify for benefits, but is also wanting to provide for a spouse, blind or disabled child, or other disabled individual, transferring those assets to a third-party trust would be a sanctionable transfer for the grantor, whereas funding a sole benefits trust would not. However, consideration should be given to the kind of benefits received by that spouse, blind or disabled child, or other disabled individual. For example, if such beneficiary is receiving Medicaid, since a sole benefit trust must payout within that beneficiary's lifetime, those sole benefit trust assets will be deemed available to such beneficiary to the extent the trustee is required to distribute and to the extent the trustee actually distributes, thereby likely disqualifying the beneficiary from Medicaid. One solution is to create a self-settled trust for the beneficiary into which those required distributions would be made. The assets in the self-settled trust would ultimately be subject to the payback provision, but the beneficiary's Medicaid could remain intact.

D. REAL PROPERTY AND ELDER LAW

Clients or potential clients often call about the wisdom of transferring their house to a child. They heard that their best friend Betty gave her house to little Johnny "so that the nursing home wouldn't come get it." While transferring the residence may actually be part of a smart benefit qualification plan, just deeding the house to little Johnny is fraught with potential problems. First, the client is transferring a valuable asset that can trigger a very long sanction period if transferred within the lookback period. Second, the client is placing their residence in the hands of another, making it subject to their decision-making, their debts, their divorces, etc. Third, the client has also just transferred his or her basis in the residence to the recipient, which could create a sizeable capital gain for that recipient if he or she wants to sell the house in the future. However, good counsel to the client can ensure that a transfer is handled in such a way that it limits or eliminates a sanction period, while still preserving the house for the applicant and his or her heirs. What may be that client's other options?

1. Life Estate Deed

a. What is it? The client transfers ownership of the real property (often residence) to a child or other beneficiary, while retaining a life interest in the property. The goal of the life estate is to protect the client from being forced out of the house or having the house sold without his or her consent.

b. How does it work for benefit purposes? By transferring the real property out of the client's estate, the real property is not available for estate recovery, while the client still retains the right to live in the property. However, this is likely a sanctionable transfer (unless it falls within an exception), so the client needs to feel as comfortable as possible that he or she will not need to qualify for Special Assistance within the next three years or Medicaid within the next five years.

2. 1% Deed

a. What is it? This is a two-step process in which the client first transfers 1% of the ownership of the real property to a child or other beneficiary as a tenant-in-common while retaining 99% ownership. The client often also retains a life estate. The second deed creates a joint tenancy with rights of survivorship between the two parties again with the client often retaining a life estate.

b. How does it work? If made as a gift, the transfer is sanctionable, but since the gift is only of 1% of the value of the property, the sanction period is dramatically shorter than with a simple life estate deed. Of course, if the beneficiary chooses to purchase the 1% interest, then it eliminates the transfer sanction. The creation of a joint tenancy with rights of survivorship by the second deed makes it such that the ownership automatically shifts to the other owner upon death (the intended beneficiary), thereby escaping estate recovery since the real property is not in the grantor's estate upon death. (Note: the untimely death of the grantee can reverse the intended consequences)

3. Ladybird Deed (Enhanced Life Estate Deed)

a. What is it? This deed is similar to a standard life estate deed, except that the client retains the right to change his mind and rescind the transfer or give the remainder interest to someone else. The basic gist of the deed would be "I, Elizabeth, give Blackacre to Richard, but I retain a life estate in Blackacre and further retain the right to cancel this deed or to give the remainder interest to any other person so named."

b. How does it work? In the above example, Richard would not pay Elizabeth or find certain value in the remainder interest because Elizabeth could always change her mind. Therefore, the remainder interest is essentially worthless. Since the remainder interest has no value, Elizabeth has not made a valuable transfer for which she can be penalized or sanctioned. Moreover, Elizabeth will likely die without changing the deed, so that Richard will automatically come into ownership of Blackacre. Therefore, upon her death, the property escapes estate recovery since it is not in Elizabeth's estate.

E. ABLE ACT

In December 2014, Congress passed the ABLE ACT (Achieving a Better Life Experience Act of 2014 - H.R. 647 113th Congress). In August 2015, Governor McCrory signed H.B. 556, North Carolina's ABLE Act. This Act allows eligible individuals with disabilities the ability to establish ABLE accounts for qualified beneficiaries. Through these ABLE accounts, people with disabilities now have control over spending for qualified expenses and making some investment decisions within the accounts, while the account itself will not disqualify the individual from Medicaid, Supplemental Security Income, or other federal benefits, provided the account is managed within the restrictions of the Act.

ABLE accounts are now available in North Carolina. Below are some quick features of ABLE accounts. If a client wants to establish an ABLE account, he or she can visit NC.SaveWithABLE.com to open the account.

1. **Basic requirements of NC ABLE Accounts**
   a. Individual must be severely disabled before the age of 26, qualification based upon either marked and severe functional limitation (certificate) or receipt of benefits under SSI or Disability Insurance (DI) programs.
   b. Individuals are limited to one account, which can be established by the disabled individual or someone acting on his or her behalf.
   c. Total annual contributions from all individuals into any one account may not exceed the annual gift tax exclusion (2018=$15,000).
      NOTE: If total amount contributed exceeds $15,000 in a year, then no long ABLE account, no longer excludable
   d. Aggregate contributions up to $100,000. Any amount in excess of $100,000 will count against individual's asset limit of $2,000
   e. Only cash contributions (some exclusion for rollover)
   f. Contributions can be made by any person, including the disabled individual
   g. Contributions are not tax deductible, but income from account is not taxable (as long as follow rules)

2. **Use and Handling of Account**
   a. Qualified expenses include any expenses made for the designated beneficiary related to their disability, such as education, housing, transportation, employment training and support, assisted technology, personal support services, health care expenses, financial management and administrative services, and other similar expenses
   b. Helps with $10,000 inheritance dilemma
   c. Helps with difficulty with remaining under resource limit (excess income/wages)

d. North Carolina Treasurer will oversee investments, offer investment options, which investments can be changed twice a year, and hold accounts for residents of NC

3. Death of Account Holder

a. Medicaid payback – based upon amounts paid after creation after Medicaid payback account

b. Any nontaxable income, if passed to remainder beneficiaries, will be taxable to beneficiaries

While ABLE accounts are a helpful option for those with disabilities and their families, they do not supplant the need for special needs trusts. ABLE account contribution and total asset limits are far more constraining than special needs trusts and will not completely serve a disabled individual's needs. However, they are a welcome tool to the benefits planning toolbox, of which we should all be aware.

F. DEMISE OF MEDICARE "IMPROVEMENT STANDARD" – Corrective Action Plan

What is the so-called "improvement standard"? After a qualifying stay in the hospital, Medicare covers the first 100 days of rehabilitative care. However, many recipients have had coverage terminated based upon their "failure to improve" while in rehabilitation. While this was never the proper standard, it had been held as the standard and followed as such until recently. The actual standard provided under federal regulations states that "the restorative potential of a patient is not the deciding factor in determining whether skilled services are needed. Even if full recovery or medical improvement is not possible, a patient may need skilled services to prevent further deterioration or preserve current capabilities." 42 CFR 409.32

Due to the prevalent use of this improper "improvement standard," in Jimmo v. Sibelius, Civil Action No. 5:11-CV-17-CR (D.Vt.) the federal court for the District of Vermont finalized a settlement among the parties, including the Centers for Medicare & Medicaid Services (CMS), which addressed the required steps to clarify and educate regarding the proper "maintenance coverage standard." As part of this Agreement, CMS agreed to undertake a program to educate all providers and contractors throughout the United States that the "failure to progress" standard is not, and has never been, an appropriate standard. This proper standard was to be communicated through the educational campaign and through revisions to the Medicare Benefit Policy Manual. Unfortunately, this education plan was not wholly effective, which resulted in a corrective action plan issued February 1, 2017 at Jimmo v. Burwell, Case No. 5:11-cv-17 (D.Vt.)

Some care facilities are indeed following the proper "maintenance coverage standard." This standard specifically holds that coverage of therapy to perform a maintenance program does not turn on the presence or absence of a beneficiary's potential for improvement from the therapy, but rather on the beneficiary's need for skilled care such as:

- ongoing assessment of rehabilitation needs and potential. [42 CFR 409.33(c)(1)]
- therapeutic exercises or activities. [42 CFR 409.33(c)(2)]
- gait evaluation and training. [42 CFR 409.33(c)(3)]
- range of motion exercises. [42 CFR 409.33(c)(4)]
- maintenance therapy. [42 CFR 409.33(c)(5)]
- ultrasound, short-wave, and microwave therapy treatment by a qualified physical therapist. [42 CFR 409.33(c)(6)]
- hot pack, hydrocollator, infrared treatments, paraffin baths, and whirlpool. [42 CFR 409.33(c)(7)]
- services of a speech pathologist or audiologist when necessary for the restoration of function in speech or hearing. [42 CFR 409.33(c)(8)]

From a practitioner's perspective, it is wise to follow-up with the client as to the reasons given for termination of Medicare benefits to ensure that the proper standard is being applied. Additionally, given the VERY short turnaround time for the appeal process, if a client calls with a termination concern, please have the client send the paperwork to his or her attorney as soon as possible to ensure that any appeal rights are secured, if necessary.