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Client Alert

A Report for clients and friends of the Firm

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This publication is a service to our clients and friends. It is designed to give only general information on the topic actually covered and is not intended to be a comprehensive summary of recent developments in the law, to treat exhaustively the subjects covered, to provide legal advice, or to render a legal opinion.

February 27, 2015

TRANSFER OF ASSETS IN MEDICAID/NURSING HOME ISSUES

This memo addresses some of the issues involved in transferring assets, typically from a parent to one or more children, in the hope that the parent will be eligible for Medicaid assistance for nursing home care. It is beyond the scope of this memo to discuss all of the details and ramifications of federal and state laws and regulations in order to determine eligibility. Rather, it is the point of this memo to discuss some of the consequences relating to such transfers, which should be considered by persons desiring to make such transfers.

I. GIFT TAX ISSUES

A. **Federal Law**. Under Federal law, you can only give a specified amount (currently $14,000) to each person, in each calendar year, without the gift being subject to federal gift taxes. Any gifts in any calendar year in excess of these limits require the filing of a federal gift tax return. If you make a gift of a "future interest" (such as a remainder interest in your home, retaining a life estate), the $14,000 per donee exemption does not apply. Typically, the gifts would be sheltered from federal gift tax by the unified credit available under federal law, but would result in a reduction of the unified credit available at your death. For many people, this many not be an issue, in that the federal unified exemption equivalent amount (including gifts) is $5,430,000 for 2015.

B. **State Law**. Historically, any gift in Tennessee over the annual exemption amount, created Tennessee gift taxes. However, for transfers after January 1, 2012, the Tennessee gift tax no longer applies. This elimination of Tennessee gift taxes removed one of the significant impediments to transfers to non-spouse family members.

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II. INCOME TAX ISSUES

A. If the transfers are of appreciated assets, then you will lose the potential of any "stepped up basis" which might be available. Currently, under federal income tax laws, if a child inherits assets from his or her parents, the child gets a new basis for that asset equal to its fair market value on date of death. If, however that same child acquires by gift from his parents appreciated property, he will "carry over" his parents' typically lower basis in the property which means that you will be subject to capital gains should you sell that asset at its appreciated value.

B. These capital gains would be totally unnecessary taxes, which would not otherwise be paid if the child simply inherited the asset from his or her parents.

III. LACK OF OWNERSHIP ISSUES

A. If a parent gives away all of his or her assets in order to qualify for Medicaid benefits, one problem is that you obviously would have no assets. *You cannot have any agreement, written or oral that your children will use those assets to take care of you*. If you have such a written or oral agreement, then that agreement itself is an asset which can disqualify you from Medicaid.

B. Even if you have an agreement with your child that they will take care of you using assets you give them, if your child refuses to honor the agreement, you will be unable to sue them in court to enforce the agreement. The court will likely take the position that such an agreement constituted Medicaid fraud. The court would likely find that you have come into court with "unclean hands", and the court would likely not permit you any remedy whatsoever. If this happens, you could not force your children to take care of you even using the assets you gave them.

IV. IF YOU TRANSFER ASSETS TO YOUR CHILDREN, THEN THOSE ASSETS WILL BECOME THEIR ASSETS.

A. If the assets belong to your children, you must consider what will happen to those assets while in the hands of your children.

B. For example, if your child dies, the assets will be in their estate and will be distributed according to their will, which may or may not cause the property to pass to someone who will take care of you with that money.

C. If your child files bankruptcy or otherwise loses the assets to a creditor, including the IRS for non-payment of taxes, no one will have access to the funds to take care of you.

D. If your child gets divorced, the assets you gave them may either be divided in the

divorce or cause your child to lose a larger share of joint assets requiring them to live more heavily out of the funds you have transferred and causing them to be unavailable to you.

V. PERIOD OF INELIGIBILITY

A. Generally speaking, if you give away assets, it creates a "period of ineligibility" before you can become eligible for any Medicaid benefits. The period of ineligibility is the time period during which an individual is not eligible to receive Medicaid benefits for nursing home or other institutional care. A period of ineligibility arises when an individual seeking Medicaid benefits has transferred money or property without fair compensation to another person or to a trust.[1] Gifts made before the "look-back period" discussed below, do not cause a "period of ineligibility".

B. The period of ineligibility is calculated by dividing the amount transferred, by the Medicaid Divestment Penalty Divisor for nursing home care (the actual cost of a particular home may be higher). As of January 12, 2015, the Tennessee Divestment Penalty Divisor is $153.02 per day and $4,591.00 per month. For example, if Mrs. Smith, who lives alone in Tullahoma, Tennessee, seeks to transfer $80,000 to her daughter (or to a trust) during the "look back period," this will create a period of ineligibility for Mrs. Smith (with respect to eligibility for Medicaid nursing home care) of Seventeen (17) months and Thirteen (13) days (rounded down to the day).

C. The DRA changed the rules regarding when the period of ineligibility begins. Prior to February 8, 2006, the penalty period for transfer began on the first day of the month following the transfer. In many cases under the old law, the period of ineligibility expired before the individual needed nursing home care. Thus, the individual's assets were saved without incurring an actual financial penalty. And, in many cases, even if an individual's assets were transferred immediately prior to going into a nursing home, a good portion of such assets could be saved in that the period of ineligibility was generally limited to Thirty-Six (36) months. However, under the DRA, the penalty period was substantially lengthened (generally, to Sixty (60) months) and begins when:

- i) the individual has applied for Medicaid;
- ii) the individual is receiving institutional care such as in a nursing home; and
- iii) the individual is eligible for Medicaid but for the penalty period.

D. An example of how the new rules affect your Medicaid eligibility would be as follows: If Mrs. Smith made the transfer set forth above to her daughter on February 28, 2014, and she entered a nursing home on December 31, 2014, and applied for Medicaid, she would not

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[1] The Deficit Reduction Act of 2005 (the "DRA") made significant changes to the area of Medicaid eligibility. In particular, the DRA seriously curtails Medicaid asset transfers and makes it much more difficult for people to become eligible for Medicaid. The DRA applies to all transfers made on or after February 8, 2006.

be Medicaid eligible until August 10, 2015 (a period of 17 months and 13 days), even if she had less than the statutory amount of non-exempt assets then in effect.

E. Finally, if you transfer all of your assets in order to avoid payment for your nursing home care, and subsequently, create a period of ineligibility, you would have no assets to take care of yourself during this period of ineligibility, plus no potential Medicaid benefits for nursing home, and therefore would be completely subject to the goodness of your children to take care of you.

VI. TRANSFERS TO A TRUST

A. If you make the transfers to a revocable or so-called "living trust", since you can revoke the trust and remove all of the assets at any time, this transfer is ignored for Medicaid purposes and you are considered the owner of all of the assets placed into the trust, the same as if no trust were created. However, any transfer of assets to a trust may result in any otherwise "exempt asset" now be countable for purposes of Medicaid eligibility (e.g. certain transfers of a residence).

B. If you make the transfer to an irrevocable trust, then it will constitute a gift and potentially create gift taxes (see gift discussion above).[2] The Medicaid rules cause all assets in the trust to be considered as available to you (and therefore an asset of yours) to the extent that the trustee has any discretion to use the trust funds for your benefit, whether or not the trustee actually uses them for your benefit. In addition, the "look back period" for counting trust assets as your assets is also Sixty (60) months.

CONCLUSION:

It is not the purpose of this memo to finalize any decision regarding making transfers to your children. Rather, it is the purpose of this article to point out problems which can arise from such transfers which are commonly not thought of by persons making transfers to their children. Our firm is frequently confronted with questions from clients who advise that "a friend" or "someone at our church" knew of someone who had conveyed away all of their assets and successfully obtained nursing home benefits. This memo is simply to point out some of the issues which can arise. While, if properly planned, some of these issues can be avoided, you still will be subject to many of the risks set forth in this memo, and must consider them carefully before deciding to make such transfers.

In light of the many issues surrounding transfer of assets in the context of Medicaid/Nursing Home issues, it is important that individuals consult a qualified attorney to help them with respect to these issues in order to ensure compliance with the law. Henry & McCord would be happy to provide such service. You may contact either James H. Henry II or John R. LaBar at (931) 455-9301 to schedule an appointment.

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[2] There are many potential gift and generation skipping tax issues which are beyond the scope of this letter.