ALEXANDER LAW OFFICES, S. C. **ATTORNEY AT LAW**
Robert G. Alexander
bob@alexander-klemmer.com
933 N. Mayfair Road, Ste. 301
Milwaukee, Wisconsin 53226

(414) 476-5020/(888) 476-8058
Fax: (414) 476-5089

TITLE XIX EXPLANATION AND PLANNING OPTIONS
FOR MARRIED COUPLES

Eligibility for Title XIX benefits is determined by considering the availability and value of all assets of both spouses, unless an asset is specifically excluded. In order to be eligible for Title XIX benefits all resources are considered available to pay the cost of nursing home care and must be spent down to pre-determined levels before a person can be eligible for Title XIX. The specific rules and levels are set forth below:

A. Assets

1. Countable, liquid resources (cash and other assets). The limits for these assets are as follows: individual in a nursing home - $2,000.00; married couple with both persons in a nursing home - $4,000.00; married couple with one person in a nursing home and the other residing in the community (known as the "community spouse") – greater of $50,000 or one-half of all countable assets up to a maximum of $109,560.00.

2. Homestead: including all related outbuildings necessary to the home's operation and all contiguous land regardless of value is exempt so long as it is the applicant's principal residence or the principal residence of the applicant's spouse or dependent relative. Once a home is unoccupied it becomes a countable resource.

3. Automobiles: One (1) automobile of any value is excluded from countable assets as long as it is used for transportation of a member of the household. If more than one vehicle is owned, the value of the vehicle with the lower value will be considered as a countable, liquid resource.

4. Life insurance policies: Life insurance policies are considered countable, liquid resources only when the combined total face value of all policies is less than $1,500.00. If the total face value of all policies exceeds $1,500.00 then the entire cash value of the policies are considered countable, liquid resources. Term insurance usually does not have cash value; therefore, it is not considered as a countable, liquid asset regardless of its face value. These rules apply per spouse.

5. Personal Property: Household goods and effects, furniture and furnishings, libraries, jewelry, and other items of personal property are not counted as long as they are not being held because of their value or as an investment.

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6. Burial Spaces, Trusts, Funds, etc.:

a. Burial spaces, including burial plots, crypts, mausoleums, urns, niches and other traditional depositories of human remains are excluded regardless of value. The exclusion also applies to contracts to purchase burial spaces as long as the contract creates a present right to utilize the space.

b. Up to $3,000.00 may be placed in an irrevocable burial trust. Interest earned on the principal may also be made irrevocable. However, funds held in an irrevocable burial trust reduce the amount dollar for dollar that may be held in a burial fund.

c. Up to $1,500.00 may be excluded (in addition to funds invested in burial spaces) for use as a revocable burial fund. The fund must be separately identifiable from other liquid resources. Interest earned on a burial fund is also excluded even if it causes the fund to exceed $1,500.00. The excludable amount in a burial fund is reduced by any amount held in an irrevocable burial trust and by the face value of all life insurance policies with cash value.

7. Subject to specific rules, income producing property can be exempted if it is used in the individual's trade or business.

Irrespective of Wisconsin's marital property law, at the beginning of a spouse's first continuous period of institutionalization, the couples' total resources from all sources are determined regardless of how assets are titled. All the couples' non-exempt resources are considered available to the institutionalized spouse except the amount considered to be the community spouse's share, which in 2008 is the greater of $50,000.00 or one-half of your combined assets up to $109,560.00. Once medical assistance eligibility is established none of the community spouse's resources are considered available to the institutionalized spouse.

Spouses need to be concerned with the amount of their total combined incomes if one of the spouses is in a nursing home and desires to make application for Title XIX benefits. The income provisions apply to all situations where one spouse is in the community and the other one is in an institution, no matter when the institutionalization begins. The "name on the instrument" rule is followed in determining available income; state marital property law is irrelevant. Income of the community spouse cannot be deemed available to the institutional spouse. In other words, no matter how much income the community spouse has, the institutionalized spouse is eligible for benefits if his or her income does not exceed the cost of his or her medical care.

If the community spouse does not have sufficient income to provide for his or her own care, the institutionalized spouse may pay part of his or her income to the community spouse. This amount is the difference (if any) between the community spouse's income and the minimum monthly maintenance allowance set by the State, which currently is the lesser of $2,739.00 or $2,333.33 plus an "excess shelter allowance" if any.

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In addition to utilizing the above exclusions and income allowances, there are a number of ways that you can plan your estate to preserve assets for yourself and your family in the event that you should require long-term nursing home care.

The following is an explanation of some of the more common methods of planning an estate so that you can qualify for Title XIX benefits.

1. You could divest your estate by making outright GIFTS to your family. Total annual gifts to any one person in excess of $13,000.00 (2009) are subject to Federal Gift Tax. However, as long as the total value of your combined estates is less than $1,000,000.00 Federal Gift Taxes will not apply since a combined "exclusion amount" will offset any Federal gift taxes. In addition, each spouse has an annual $13,000.00 (2009) per year, per donee, exemption from any gift tax which is applied prior to use of the exclusion amount.

When gifting assets there are several income tax issues that must be carefully considered relating to the "tax basis" in your property. The tax basis is generally defined as the purchase price of the asset less depreciation. The tax basis of gifted property is a "carry over" basis. This means that the donee's tax basis in the property is the same as the donor's tax basis as of the date of the gift. The basis of property received on death is "stepped up" to the fair market value of the property as of the date of death. Therefore, if you gift appreciated property outright to your family members or into a trust there will be an income tax consequence to the family members or to the trust when the asset is eventually sold. Tax will be due on the difference between the fair market value of the asset when sold and its "carry over" basis. Assets will receive a step up in basis to fair market value at date of death if the assets are held until death; therefore, income tax consequences are generally eliminated.

Additionally, if your home is gifted, you can lose the opportunity to use the exclusion of gain on the sale of the home.

2. ANNUITIES are extremely useful planning tools because of their flexibility and because they can be used to gain eligibility for Title XIX benefits without a long waiting period. Annuities can be commercial annuities (i.e. a life insurance product) or private annuities (i.e. setup with your family or estate plan). An annuity is not considered a countable resource once the annuity has annuitized, provided it is annuitized over the life expectancy of the annuitant as determined by the State of Wisconsin. That means that you would be receiving the principal from the annuity. You must be careful to be sure that the annuity payments themselves do not count as a resource. If the annuity has not annuitized, the entire value of the annuity is considered a countable resource. Oftentimes annuities are gifted, but if they are gifted you must be aware that the excess of the present cash value of the annuity over its cost basis is subject to present income taxation. This must be taken into account when gifting annuities.

Several additional considerations with respect to annuities have been incorporated into Wisconsin Law as of March 1, 2004 and the new DRA rules:

1. In order for an annuity to be considered an exempt assets, the annuity must be an immediate annuity, rather than a tax-deferred annuity.

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2. Medical Assistance Qualified Annuity must be irrevocable. The “irrevocable test” is satisfied by showing that the Medical Assistance Qualified Annuity is an immediate annuity, rather that a tax-deferred annuity. The terms of the payment, as well as the parties, cannot be changed or altered.

3. It must be actuarially sound. The “actuarially sound test” is satisfied by structuring the Medical Assistance Qualified Annuity payout over a period of time, no longer than the individual’s Medical Assistance lifetime. An individual’s Medical Assistance lifetime is defined in the Wisconsin Medicaid Eligibility Handbook.

4. It must be non-assignable, and non-surrenderable. The “non-assignable/non-surrenderable test” is satisfied by having the Medical Assistance Qualified Annuity contract structured so that it cannot be sold, transferred or assigned for value, to any third party.

5. It must make fixed, periodic payments. The “fixed and periodic payment test” is generally satisfied by structuring the Medical Assistance Qualified Annuity payout with equal monthly payments.

6. It must generate a minimum rate of return. The “minimum rate of return test” is satisfied by having the Medical Assistance Qualified Annuity meet the Applicable Federal Rate for the month in which the annuity is structured.

7. It must not have any value on the secondary market. The “not having any value on the secondary annuity market test” is satisfied by providing documentation from three (3) independent companies, which are active in the secondary annuity buyers market, of their unwillingness to purchase the Medical Assistance Qualified Annuity .

8. With Wisconsin's new rules, private annuities will be required to include a provision listing the State of Wisconsin as the beneficiary of the annuity upon the death of the annuitant (in an amount equal to the total benefits provided by the state).

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A Medical Assistance Qualified Annuity which is specifically structured to provide that the annuity is irrevocable, and that neither the contract nor its stream of income payments can be assigned, transferred or surrendered.

3. A LIFE ESTATE is not a countable resources regardless of its value. A life estate is a split form of ownership. Property is gifted to others (i.e. family members) with the donor retaining the right to the use of the property for whatever period of time the donor desires. The gift of the remainder interest (the value of the property interest gifted away) is subject to the federal gift tax issues discussed above. The gift of the remainder interest is also a divestment which may make you ineligible for Title XIX benefits for a period of time equal to the lesser of (a) sixty (60) months from the date of the transfer or (b) the number of months arrived at by dividing the amount transferred by $6,259.00. The advantage of a life estate is that it allows the owner to use the property (i.e. a home) as long as he or she would like to, thereby maintaining control over the property as long as he or she lives. Once the property is abandoned or the original owner passes away, the life estate terminates and ownership of the property then passes entirely to the family members or whomever else the property has been gifted to.

While life estates are often used in Title XIX planning, there are some distinct disadvantages. If property is sold, it requires the signature of the donor and all donees. The donee's interest in the property is subject to risk of loss due to divorce, death, legal incompetency, or creditor problems of the donee. Also, if the property is sold during the lifetime of the donor a portion of the proceeds is paid to the donor and the rest is paid to the donee; in either case, this may not be what you want and could cause a real problem. Not only does this cause a risk of loss of the funds from the donor to the donee, but it can also bring a portion of the asset back into the donor's estate, contrary to the initial intent of Title XIX planning. Also, you need to carefully consider the income, gift, and estate tax consequence of using a life estate, including, but not limited to a partial loss of the once in a lifetime exclusion of income on the sale of a personal residence. Finally, one of the drawbacks of a life estate is that the donee has a carryover basis in the gifted portion of the property. Therefore, if the property is sold or transferred during the donor's lifetime, there can be tax consequences to the donee.

4. You can establish an IRREVOCABLE TRUST with the option of having the trust pay income to you during your lifetime. However, if you reserve the right to the income, the income payments will count as income for purposes of determining Title XIX eligibility. As long as you have no ability to receive the principal, the principal will not be considered a countable resource. If you do not retain the right to the income, the income is not a countable resource. Gifts to the trust are subject to the same gift tax issues outlined above. The advantage of this plan is that after a gift has been made, and after the appropriate waiting period has passed before you can be eligible for Title XIX benefits (generally a maximum of sixty months, subject to special rules regarding trusts), the entire principal is preserved for your family and heirs. It is possible to draft a provision in the trust to the effect that the principal and/or income of the trust can be used for the benefit of the family in the discretion of the Trustees. The family can then, if they so wish, make gifts back to you over and above the benefits that Title XIX is providing or they can pay expenses on your behalf. One of the principle advantages of this type of trust is the control that you can maintain over this trust during your lifetime without having the assets includable as

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resources for the purpose of Title XIX eligibility. Also, the trust can be structured so that the income and gift tax problems with respect to gifting property can be eliminated. All of the assets gifted to the trust will receive a step up in basis to fair market value at date of death, and homesteads will still be eligible for the exclusion from income tax on the sale of the house. This can be a tremendous tax advantage to your family. Irrevocable trusts are often combined with annuities. This combination often allows you to maintain control over the assets, allows flexibility in planning, eliminates the tax problems often associated with most plans, and can allow a person in a nursing home to qualify for Title XIX benefits without a long waiting period.

5. You could make outright gifts to your family subject to the gift tax issues discussed above. The family could then gift the assets into an irrevocable trust that the family members establish. All of the income and principal of this trust could be made available in the discretion of the Trustee to pay for your care over and above what Title XIX is providing. A trust established by the family members is not considered a countable resource for purposes of Title XIX since it is not established by you. However, care must be exercised so that it does not appear that the gifts from you to family members, and the gifts from the family members to the trust are simultaneous such that the appropriate reviewing agencies would consider each of these steps part of one overall transaction. This would cause a serious risk of loss of your assets, especially under new federal and state laws. Also, there is no way you can legally force your family members (or trustees, if your family members are trustees of a trust created for your benefit) to provide for you. Gifts to the trust by the family members are also subject to the gift tax rules outlined above and must be carefully coordinated with each family member's individual estate and tax planning.

6. You could establish a FAMILY LIMITED LIABILITY (LLC) COMPANY. A family limited liability company is a business and estate planning entity, first authorized by Wisconsin Statutes as of January 1, 1994. The family limited liability company works like a family limited partnership; that is, assets are protected from creditors, including the government, yet all the income is taxed to the owners as individuals. A limited liability company is set up by you as the organizer. You transfer the assets that you want protected to the limited liability company, which is owned by yourself and designated third parties, such as family members. Control of the daily operations of the limited liability company are delegated to managers responsible for the daily operations of the limited liability company. This is usually yourselves as the persons who organize the LLC. Members of the LLC are not generally liable for LLC debts. Assets placed in the LLC are exempt from the claims of creditors including the government. This is true not only for yourselves as the organizers of the company, but also assets are not subject to risk of loss by family members or the other members of the LLC, i.e., I.R.S., divorce, disability, incompetency, family, and other legal problems. Income from the LLC can be allocated to the persons who establish the LLC so that you may have use of the income during your lifetime. Through your voting control over the LLC, you retain the control, use, and enjoyment of the assets within the LLC. Distributions of principal can be made directly from the LLC to you, but this will require the vote of not only yourself, but also of at least one other company member who is not your spouse. This restriction on direct retransfer of principal back to yourself is what makes the assets unavailable for purposes of determining Title XIX eligibility. Obviously, within a family context, there should be no difficultly in distributing assets back to yourself, since the whole purpose in establishing a trust, an LLC, or any other "Title XIX" plan is to ensure that the family

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works together as a unit, but not subject the assets which are being protected to risk of loss either on your own behalf or because of unfortunate events in the lives of your children or their families. Upon the death of the organizer (person establishing the LLC), the LLC can be liquidated and the assets distributed to appropriate family members or other designated beneficiaries without probate.

7. You can divest (gift) $6,258.00 per month. Please note that this is one dollar less than the figure that is used to calculate the divestment penalty (which is $6,259.00). A transfer of $6,258.00 per month does not trigger any period of ineligibility for Title XIX benefits due to the formula by which ineligibility is determined by the State of Wisconsin.

One of the major advantages of making gifts to an irrevocable trust or a family limited liability company is that the assets are not available to the family members for their use and therefore are not subject to the claims of their creditors, marital dissolution, death, or the fact that the family members may simply choose to spend the money for their own benefit to the exclusion of the parent (as often happens).

In addition to some of the gift and income tax issues discussed above, the disadvantage of outright gifts to family members is that you lose control over the assets. The assets are no longer yours. Therefore, you must have explicit faith in your family members as donees to take care of you and meet your needs in the future. However, there are provisions that can be drafted into the trust outlined in paragraph four (4) above that allow you to maintain control over the distribution of assets to the family members. Also, the LLC outlined in paragraph six (6) above will allow you to maintain control over how the assets are invested and reinvested and control the distribution of assets to yourself and your family members. Properly drafted Trusts and LLC's can be effective tools to allow you to maintain control over your assets and guarantee that your assets are used as you plan and are not squandered, seized, or lost against your wishes.

NOTE: If you divest (gift) all or any portion of your assets you may be ineligible for Title XIX benefits for a period equal to the lesser of a) sixty (60) months from the date of the transfer or b) the number of months arrived at by dividing the amount divested by $6,259.00. Therefore, the timing of any plan must be carefully coordinated with this rule to reduce the possibility of losing any benefits. Also, the sixty month period can be extended to sixty months for transfers involving certain types of trusts. Note that the ineligibility period can be indefinite depending upon the time when an application for benefits is filed. Finally, remember that these rules have been changed by the Federal DRA legislation, changes ultimately which will be incorporated into Wisconsin law.

There are several possible additional consequences of divestment that need to be addressed. First, there can be a loss of privacy if divestment is made. Reports and accountings are required by the administrating agency and there are periodic reviews and evaluations intruding into one's private life and family information.

Second, there is a loss of independence and control. If divestment is prior to the need for institutionalization, you may run out of funds for living expenses outside of an institution (including any needed home based care). If divestment is found and the person is ineligible for

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benefits but in need of institutional care with no resources left, he or she may not have means to pay for nursing home care. Additionally, you can lose the choice of a particular nursing home since a person can only receive care in a certified facility.

Third, there is the possibility of discrimination by care providers against Title XIX patients, including, but not limited to, discrimination in admission policies, difference in standard of care between private patients and Title XIX patients, undesirable assignments of location and indiscriminate transfers within a nursing home facility affecting access to the patient and level of care.

Fourth, nursing home Title XIX certification can terminate. Also, a home could choose to or be forced to decertify its Title XIX patients. A resulting transfer could cause inconvenience, trauma and new patient access problems.

Fifth, the level of care needed by an individual may change, i.e. the condition could improve so that the level of care needed is down graded causing ineligibility for Title XIX.

Sixth, the Title XIX program can change in the future affecting eligibility requirements and could also affect the rules and planning devices we have discussed above.

While these consequences can be greatly reduced or eliminated by property planning, they do need to be considered before establishing any plan.

Please realize that the rules regarding these planning techniques can be <u>very</u> <u>complicated</u> and in some cases the family is going to have to make some <u>difficult</u> <u>choices</u> if you wish to protect your assets in the event that you enter a nursing home. Therefore, after you review this letter I recommend that you give me a call and I can answer your questions and fill in some of the specifics which may not have been included in this information.

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