Trusts & Estates

IN THIS ISSUE

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Victor Case Impacts Use of Certain Trusts in Planning for Medicaid Eligibility

BY JANET W. MOORE

Trusts are valuable and popular tools often used in estate planning; however, trusts can also create problems when attempting to plan and qualify for Medicaid (MassHealth) for payment of long term nursing home care.

In general, assets held in a trust are considered "countable" and "accessible" (and therefore must be spent down prior to qualification for MassHealth) if the assets can be made available to the individual who is applying for MassHealth. The rules regarding MassHealth financial eligibility apply to trusts that are "created or funded by the individual or spouse, other than by a Will." 130 CMR 520.022(B)(C). Under this definition, a spouse can leave assets to his or her surviving spouse in a trust created as part of his or her Will (a "Testamentary Trust"). The surviving spouse can then have the benefit of the assets in a Testamentary Trust and still qualify for Medicaid.

What if the trust were created instead in a stand-alone trust outside of the Will (an Intervivos or Living Trust)? This type of trust is widely used in estate planning in Massachusetts. Practitioners have wondered and logically felt, that if a Living Trust were established but not "funded" until the spouse died, the assets pouring-over to the trust from the Will (i.e., funded by the Will) would also be protected and the surviving spouse could qualify for MassHealth. Most practitioners drafted estate plans relying on this premise and in the past MassHealth accepted this.

In July, however, the Massachusetts Appeals Court decided this issue in favor of MassHealth. (Victor vs. Massachusetts Executive Office of Health and Human Services, 2010 Mass. App. Unpub. Lexis 844.) In Victor, prior to the deceased spouse's death, a Living Trust was created and funded with only $10 and was the named beneficiary of a life insurance policy that never was paid to the trust. The decedent's Will poured over $160,000 of probate estate assets to this trust. The family argued that the trust was, therefore, funded by the decedent's Will. The Court disagreed with the family and ruled in favor of MassHealth by holding that the

Victor Case, continued on page 2

Victor Case, continued from page 1

trust was "created or funded other than by a Will." The $160,000 was, therefore, a countable and accessible asset of the surviving spouse, who was denied MassHealth benefits until the $160,000 was "spent down."

In light of the Victor decision, it is extremely important for your estate plan to be reviewed and updated if your estate plan contains a pour-over Will and Living Trust and is expected to protect assets from being countable to a surviving spouse for MassHealth asset protection planning. ■

Making the Best of a Bad Situation: When MassHealth Places a Lien on Your Home

BY ARTHUR P. BERGERON

No one wants to have to go to a nursing home. Most people would much rather remain in the familiar surroundings of their home. However, for those individuals who need to be in a nursing home for the long term, life is made worse by the fact that Medicare does not cover the cost, which in Massachusetts, is between $9,000 and $12,000 per month!

While you can generally qualify for MassHealth (the one government program in Massachusetts that does pay for the cost of long-term nursing home care) even when you still own a home, you must, however, agree to sell it. Furthermore, MassHealth will place a lien on your home to ensure that when the property eventually is sold, MassHealth will recover the amount it has paid for nursing home care on your behalf. While only advanced planning (typically five years in advance) will allow you to avoid this situation completely, there are ways you can make the best of this bad situation.

…while long-term advanced planning is best…it is worthwhile to explore strategies that can keep a bad situation from becoming even worse.

In an attempt to encourage people to sell their home and repay MassHealth, several years ago MassHealth adopted a regulation requiring MassHealth recipients to accept any offer to purchase their home equal to at least two-thirds (2/3) of the current fair market value of the home. While the fair market value is presumed to be the assessed value, the MassHealth recipient can rebut this presumption with an appraisal. While at first blush this seems to be bad news because it forces people in nursing homes receiving MassHealth benefits to sell their homes at fire-sale prices, it can also be good news in some situations.

First, even if it is your child who offers to purchase the home for two-thirds (2/3) of its value, you not only ***can*** accept the offer, but you ***must*** accept the offer. It does not matter if your child subsequently resells the home for its full value. This is true even though MassHealth recipients cannot make any gifts to their children.

Next, this plan can still make sense for people who have been in a nursing home for a long time and who own homes on which the MassHealth lien exceeds the property's value. Because the regulation requires the acceptance of a purchase price that is at least two-thirds (2/3) of fair market value, MassHealth would be required to release its lien for this lower price; thus saving some equity in the home for family members.

Finally, the regulation requiring the acceptance of the at least two-thirds (2/3) offer is applicable irrespective of whether there are any outstanding mortgages on the property. Therefore, a nursing home resident owning a home worth $300,000 that is subject to a reverse mortgage with a pay off of $200,000 could sell the property to a child for $200,000, payoff the mortgage, and effectively transfer all of the equity in the house to the child.

The moral is this: while long-term advanced planning is best, and while nothing can reduce the pain and angst that inevitably accompanies the decision to place a loved one in a nursing home, it is worthwhile to explore strategies that can keep a bad situation from becoming even worse. ■

Important Tax Provisions in the 2010 Health Reform Legislation: What You Need to Know

BY ANDREW B. O'DONNELL

This past March Congress enacted sweeping health care reform that will significantly affect the way health care is administered and paid for in the United States. In order to pay for the cost of health care reform, several tax provisions were included in the legislation. This article will highlight some of the key tax provisions.

Increased Medicare Tax for High Income Taxpayers

Beginning in 2013, there will be an additional .9% Medicare tax on certain wages and self-employment income. Under current law, all employees pay a 1.45% Medicare payroll tax on their wages, and their employer pays an additional 1.45% on behalf of the employee. Self-employed individuals are responsible for paying the entire 2.9% Medicare tax on their earnings.

Under the new law, single taxpayers earning more than $200,000 per year and married couples earning more than $250,000 per year will be subject to an additional .9% Medicare tax on wages in excess of those threshold amounts. As a result, the excess amounts will be subject to a total 2.35% Medicare tax. Self-employed individuals will pay the entire 3.8% Medicare tax on wages in excess of the thresholds. Neither of the thresholds will be indexed for inflation. In addition, for married couples filing joint returns, the new .9% additional Medicare tax will be imposed on the couple's combined wages in excess of the $250,000 per year, not in reference to each spouse's individual wages above $200,000 per year.

The new .9% Medicare tax will not apply to the share of the Medicare tax paid by employers; they will continue to be required to pay the current 1.45% Medicare tax. However, the employer will be required to withhold the additional .9% tax imposed on employees from employee wages for those employees who earn more than the threshold amount of $200,000 per year. The employer is not required to take into account any wages earned by the employee's spouse in determining whether or not the combined wages of the employee and his or her spouse exceeds the applicable threshold amount of $250,000. This may result in under-withholding for certain married couples, resulting in additional Medicare taxes owed when their income tax return is filed.

Finally, the additional .9% Medicare tax imposed on self-employed individuals will not be eligible for the current income tax deduction available to self-employed individuals for 50% of self-employment taxes paid.

New Medicare Tax on Net Investment Income

Beginning in 2013, investment income earned by individuals will be subject to a new 3.8% Medicare tax on net investment income. This new tax will apply only to single taxpayers with adjusted gross income above $200,000 and married couples filing jointly with adjusted gross income in excess of $250,000. Neither of these thresholds will be indexed for inflation. This new 3.8% Medicare tax is in addition to the .9% additional Medicare tax (discussed previously) that is imposed on wages and self-employment income.

Net investment income is defined as income from interest, dividends, royalties, rents, passive income, and gain from the sale of property that is not used in trade or business. A taxpayer is allowed to reduce his investment income by any deductions allocable to the production of this income. Fortunately, distributions from qualified retirement plans are not treated as investment income for purposes of this 3.8% tax.

Unfortunately, the calculation of the tax is complicated. The tax applies to the lesser of (i) net investment income, or (ii) adjusted gross income (with certain modifications) in excess of the applicable threshold amount of $200,000 or $250,000. As a result, taxpayers with significant adjusted gross income are likely to have most of their net investment income subject to this new tax.

> **Example:** *A single individual has adjusted gross income of $230,000 and net investment income of $50,000. The taxpayer will be required to pay the new 3.8% Medicare tax on $30,000 of his investment income since this is the amount by which the adjusted gross income ($230,000) exceeds the applicable threshold ($200,000).*

> **Example:** *A single individual has adjusted gross income of $350,000 and net investment income of $50,000. In this scenario, the taxpayer would be required to pay the new 3.8% Medicare tax on all $50,000 of the investment income since the tax is imposed on the lesser of the net investment income ($50,000) and the amount by which the adjusted gross income of $350,000 exceeds the applicable threshold of $200,000 ($150,000).*

Additional Deduction for Self-Employed Individuals

Effective March 30, 2010, self-employed individuals can now deduct the cost of health insurance paid for by the taxpayer that is provided to a child who has not attained the age of 27 as of the end of the tax year even though the child no longer may qualify as the taxpayer's dependent.

Dependent Coverage in Employer Health Plans

The new legislation makes a complementary change to the rules governing the income taxation of employees with respect to health insurance benefits provided to the employee's children under an employer-provided health plan. Under the new rules, the exclusion from income for benefits provided under these plans is extended to any child of an employee who has not attained age 27 as of the end of the tax year involved.

Medical Expense Floor Raised

Under current law, an individual who itemizes his or her deductions can deduct unreimbursed medical expenses to the extent that these expenses exceed 7.5% of the individual's adjusted gross income. The new legislation increases this floor from 7.5% to 10% beginning January 1, 2013, thereby making it more difficult to deduct these expenses. However, the current threshold remains in effect through December 31, 2016 for taxpayers who are age 65 or older (or whose spouse is age 65 or older) in any tax year prior to 2017.

> **Example:** *A taxpayer is age 64 at the end of calendar year 2013. As a result, he or she will be subject to the 10% floor in that year. However, for tax years 2014 through 2016, he or she will be subject to the 7.5% floor in each of those years since he or she will be age 65 or older. Beginning in 2017, the taxpayer once again will become subject to the 10% floor.*

Changes for Flexible Spending Accounts and Health Savings Accounts

Currently, funds in flexible spending accounts and health savings accounts can be used to pay for the cost of over-the-counter medications. Beginning in 2011, paying for the cost of over-the-counter medications from these accounts will be banned. In addition, the penalty for nonqualified distributions from health savings accounts will be doubled, from 10% to 20%. Beginning in 2013, amounts that employees can contribute to flexible spending accounts will be capped at $2,500 per year. Previously, the employer could choose the amount an employee could contribute to the flexible spending account. No such limit is imposed on health savings accounts.

W-2 Reporting by Employers

Effective January 1, 2012, an employer must now report the value of all health insurance benefits provided by the employer on each employee's Form W-2.

Reporting of Foreign Financial Assets

The current rules that require individuals to report foreign bank accounts when the aggregate value of the accounts exceeds $10,000 have now been made part of the tax code. Effective in 2011, individuals who own an interest in "foreign financial assets" with an aggregate value greater than $50,000 must attach a disclosure statement to their income tax return reporting these accounts. Failure to do so will subject the taxpayer to a penalty of $10,000, with the potential for additional penalties if non-disclosure is not corrected in a timely manner after notice from the IRS.

In a related change, the new legislation revises the accuracy-related penalties imposed with respect to understatements of tax that are attributable to undisclosed foreign financial assets. As revised, the penalty has increased from 20% to 40% of the tax underpayment relating to the unreported foreign account. ■

Joint Bank Accounts: the Solution or the Problem?

BY PATRICIA L. DAVIDSON

Though commonly used, joint bank accounts can often cause family disputes, and at times, even lead to litigation. Typically, an older person names a younger person as a joint owner on an account. When the older person dies, the question arises whether the surviving joint account holder should inherit the account or the account should pass as part of the probate estate. In fact, whether the account belongs to the survivor or to the estate is one of the most common legal issues that may arise after the death of a family member.

Generally, joint account holders are co-owners of the bank account and have equal rights to access money in the account. Additionally, upon the death of one of the joint owners (the "decedent"), the survivor is presumed to be the owner of the money in the account and the account is presumed not to be part of the assets of the decedent's probate estate. This presumption, however, is rebuttable with sufficient evidence that the decedent did not intend the survivor to inherit the

account. The executor (if there is a will) or the administrator (if there is no will) of the estate has the responsibility to try to recoup the money if he or she believes that the decedent intended the money to pass as part of the probate estate. To do so, the executor or administrator may need to file a lawsuit against the surviving joint account holder.

Consider the following example:

> *Mom has two children, Ann and Tom. Mom is showing signs of slowing down and her memory, particularly her short-term memory, is failing. She has "good days" and "bad days." Mom puts Ann's name on Mom's bank account totaling $100,000 so it is easier for Ann to help Mom with her banking. A couple of years later, Mom passes away. Mom has a will that leaves her remaining assets, totaling about $50,000, equally to Ann and Tom. Bob is the executor of Mom's estate. Is Ann entitled to keep the money in the bank account, or do Tom and Bob have a claim that the $100,000 should be part of the estate and divided equally between Ann and Tom?*

As a starting point, Bob presumes that Ann is entitled to the money in the joint account. Tom, however, may argue that Mom only made Ann a joint account holder "for convenience," so that Ann could more easily assist Mom with her day-to-day banking needs and that Mom did not intend for Ann to benefit from the account, to the exclusion of Tom. Courts have often ruled that if the purpose of the joint ownership is to facilitate making deposits, writing checks, and transferring money between accounts, the primary account holder did not intend that the joint account holder benefit from the money. If Bob agrees with Tom, Bob can ask Ann to turn over the account to the probate estate. If Ann refuses, Bob will need to sue Ann to return the account to Mom's estate.

Tom may also stress that Mom lacked legal capacity when she made Ann a joint account holder. He may argue that Mom was experiencing confusion or memory loss and did not understand the consequences of her actions. If Bob can produce medical or other evidence of Mom's inability to understand the nature of her actions at the time Ann became a joint account holder, a court may determine that the money belongs to Mom's estate and not to Ann.

Tom may also argue that Mom was vulnerable and that Ann coerced Mom into putting Ann's name on the account. Tom may try to show that Ann exerted "undue influence" upon Mom to cause Mom to change the account. Tom may argue that Mom never would have changed the account if Ann had not somehow pressured her or misled her about the consequence of making Ann a joint account holder. If Bob can uncover evidence to support the claim, a court could order Ann to turn over the money to Mom's estate.

Since there is a presumption that Ann is the legal owner after Mom's death, Bob would have to come forward with specific evidence supporting his allegations that (i) the account was for convenience only, (ii) Mom lacked capacity, or (iii) Ann engaged in undue influence. While it is easy to speculate about Mom's intent or Ann's improper actions, it can be very difficult to obtain credible documents or testimony to challenge the joint account holder's survivorship rights. Often the two joint account holders are the only ones who were privy to conversations and circumstances concerning the creation and operation of the bank account. If the primary account holder is infirm or has died, and the surviving account holder lies or is self-serving, it can be difficult to challenge the survivor's presumptive rights.

Ultimately, when assessing who is entitled to a joint bank account, a court will focus on the primary account holder's intent. The court would likely consider Mom's past practice, her banking habits, statements that she made to Ann, Tom or others close to her, or whether she gave any specific indication that she intended Ann to be the owner of the account upon her death.

To avoid ambiguities and to minimize the chance of a family dispute, a primary account holder should communicate his or her intent in writing to family members, bankers, accountants, attorneys, or any other advisors involved. Attorneys, in particular, can explain the consequences of a joint bank account and can provide other estate planning solutions to minimize potential battles over joint bank accounts. For example, language can be put in a will indicating that any joint accounts are presumed to be for convenience, or that all assets in joint accounts should be considered part of the probate estate to be distributed in accordance with the will.

Joint accounts are a very common way of not only managing money, but also transferring money in the event of an account holder's death because they are a simple and inexpensive way of avoiding probate. But joint accounts are also the cause of much animosity and resentment in families and can lead to accusations that the surviving joint account holder engaged in wrongdoing. Whether your primary assets consist mainly of bank accounts or whether your bank accounts are just a small portion of a larger estate, it is prudent to discuss with your attorney the consequences of having more than one name on any bank account. ■

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ABOUT US

Attorneys in the Mirick O'Connell Trusts and Estates Group counsel individuals and families in all matters concerning estate, gift, charitable and fiduciary income tax planning, elder law and special needs planning, and asset protection and Medicaid planning.

Our attorneys have extensive experience in drafting sophisticated estate planning documents and implementing wealth planning strategies. The integration of our experienced trusts and estates lawyers with our skillful litigation and trial lawyers enables us to provide sound legal advice and creative dispute resolution strategies.

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This overview is intended to inform our clients of developments in the law and to provide information of general interest. It is not intended to constitute legal advice regarding a client's specific legal problems and should not be relied upon as such. This newsletter may be considered advertising under the rules of the Massachusetts Supreme Judicial Court.

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