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Factors to Consider When Converting Excess Resources Into an Income Stream for Purposes of the Institutional Medicaid "Snapshot"

By Regina Kiperman and Naomi Levin

Jack and Alice are married. Jack is 80 years old. He is sick, requires institutional care, and is about to enter a nursing home. (Jack is the "Institutionalized Spouse.") Alice is 75 years old. (Alice is the "Community Spouse.") Jack and Alice have a house, free and clear of mortgage and $750,000 worth of investable assets, generating de minimis annual income in the form of dividends (estimated at $4,000 a year). Each spouse also has their own separate IRA in payout status. The Institutional Spouse's required minimum distribution is $750 a month. The Community Spouse's required minimum distribution is $200 a month. The Institutional Spouse receives $2,000 a month from Social Security while the Community Spouse receives $510 a month from Social Security.

Jack and Alice come to you for Medicaid planning. You know that transfers between spouses are exempt.[1] If Jack transfers all of his assets to Alice, Jack can thereafter apply and be eligible for Medicaid. You also know that the Community Spouse may execute a "Spousal Refusal" advising the Local Department of Social Services ("DSS") that the community spouse refuses to fulfill his/her obligations, as the legally responsible relative, to support the institutionalized spouse.[2] DSS will provide the necessary medical assistance to the institutionalized spouse, notwithstanding the community spouse's refusal to contribute to the cost of the institutionalized spouse's care. However, the filing of the "spouse refusal" may create an implied contract with DSS, authorizing DSS to commence a claim for spousal contribution from the community spouse for the cost of care paid by DSS for the benefit of the institutionalized spouse.[3] [4] When initiating a claim for spousal contribution, DSS will look to the community spouse's income and/or resources in excess of applicable limits.

Current laws permit the Community Spouse to retain monthly income up to the amount of the minimum monthly maintenance needs allowance ("MMMNA"), and resources up to the amount of the community spouse resource allowance ("CSRA").[5] The MMMNA[6] and CSRA[7] are exempt from recovery by DSS and are adjusted annually to account for increases in cost of living.[8] Income and resources above the MMMNA and CSRA may be subject to a contribution claim from DSS. Currently, New York State limits its claims for spousal income contribution to twenty-five percent (25%) of the Community Spouse's income in excess of the MMMNA.[9] (The amount sought for contribution may be reduced if the Community Spouse can demonstrate a need for an increased income allowance, and therefore an increase in the MMMNA.)[10]

You know that the Community Spouse can have a Federal CSRA of $119,220 (and an MMMNA of $2,980.50) in 2016.[11] Thus, if Jack keeps $14,000 in his own name and transfers the balance to Alice, the first $119,220 in 2016 can be held free and clear of any contribution claims. Unlike the contribution claims for income, however, there is no limit on how much DSS can request for contribution of excess resources over and above the CSRA. Therefore, you are left wondering what can you do to protect your client's excess resources? Put another way, should you convert the excess resources into income so that you can mitigate the amount of money subject to contribution to just 25% of the income over the MMMNA?

You have heard suggestions regarding converting the excess resources over the CSRA into an income stream by using either a Promissory Note[12] or Medicaid Compliant Annuity[13] before filing the Medicaid application.[14] The goal of this approach is to provide a snapshot that minimizes, if not completely eliminates, the excess resources. Instead, the result of the conversion of the excess resource into an income stream will be that the snapshot will show a higher income stream (which is exposed to a maximum contribution claim of 25%). Should you employ this technique, you wonder?

This tool may not always be the optimal approach for your clients. Therefore, before you engage this method, you should conduct a cost/benefit analysis and consider the following.

1. Effect of the conversion on potential spousal impoverishment budgeting

When a community spouse earns less than the MMMNA, once Medicaid eligibility has been established for the institutional spouse, the community spouse can request spousal impoverishment budgeting wherein the institutional spouse's income is allocated to the community spouse such that the community spouse's income is brought up to the MMMNA.[15] The amount of income allocated is referred to as the Community Spouse Monthly Income Allowance ("CSMIA").

In our example, Alice's total monthly income (from Social Security, dividends, and her IRA distribution) does not equal or exceed the 2016 MMMNA of $2,980.50. Therefore, after Jack is determined eligible for institutional Medicaid, Alice may request that a portion of Jack's income be allocated to Alice. (In this instance, Jack can have almost $2,000 allocated to herself from Jack's income). However, if Alice converts all of her excess resources (approximately $650,000) into an income stream, it is very likely that the additional income will push her total monthly income over the MMMNA, and she will no longer be eligible to receive a CSMIA from Jack's income. Instead, Jack's income may be paid to the nursing home. Furthermore, the DSS may bring a contribution claim, requesting a contribution of 25% of Alice's income in excess of the MMMNA.

It may make sense to ask yourself the following questions: Is the Community Spouse eligible for minimum monthly maintenance needs allowance ("MMMNA") from the Institutionalized Spouse? If so, will the creation of the promissory note completely eliminate the amount of the MMMNA? Will it reduce the amount of the MMMNA? Is the Community Spouse better off receiving the MMMNA from the Institutional Spouse and possibly using some of the MMMNA as a negotiation tactic with DSS?

2. What is your client's risk tolerance?

A client who prefers certainty may find limiting potential liability to 25% of their income in excess of the MMMNA quite appealing. Indeed, risk-averse clients may prefer to have a calculation of their exact liability and may even want to make a voluntary contribution,[16] rather than waiting for Medicaid to file the claim.

Clients who are more risk tolerant may want to take their chances. In our example, Alice, who will ultimately seek spousal budgeting, may be better off not converting her excess resources on the theory that DSS may see her relatively lower income and overlook her excess resources. Alice, if she is more risk tolerant, may choose to wait to see what, if any steps, DSS takes.

3. What is the term of the note?

A non-qualified annuity or promissory note must be actuarially sound as determined in accordance with actuarial publications of the Office of the Chief Actuary of the Social Security Administration.[17] The longer the term of the note, the lower the income. At the end of the day you are tying up your client's funds. The question is—for how long?

Factors to consider include:

- What are the actuarial life expectancies of the spouses?
- What are the realistic life expectancies of the spouses (based on the health/medical conditions of your specific clients)?[18]

For example, if the institutional spouse is terminal and has less than six months to live, perhaps the community spouse may not want to enter into an irrevocable agreement restricting access to resources for a period of time greater than six months. In situations such as these, it may be important to speak with the institutional spouse's care-team, as well as to check the actuarial life expectancy tables to understand the term of the note.

Reverting back to Jack and Alice, Alice's life expectancy (at age 75) is 12.76 while Jack's is 9.58. A note for the term of Alice's life expectancy would be "actuarially sound," but might result in income payments beyond Jack's life (and need for Medicaid benefits). Would Alice prefer to have her assets returned to her more quickly? Does the existence of the note and income stream create future problems for Alice's own future Medicaid eligibility and planning, or for her estate?

4. How much of the community spouse's resources should be converted into an income stream?

Should the community spouse convert all of her excess resources into an income stream? Should she convert more than her excess? Or perhaps she should only convert some of the excess.

Consider your client's needs and wishes. Does the community spouse need access to large amounts of money in the near future, or can she meet all of her needs with an income stream? Consider both anticipated and unanticipated needs that might arise, including things like vacations, home improvements, education for grandchildren, and medical emergencies.

5. Is there a correlation in your region between a lower "excess resource" amount and the chance that your local DSS will pursue a contribution claim?

Speak to your colleagues, the local DSS, and review any fair hearings. Perhaps there is a trend in Suffolk County such that Suffolk County pursues everything. Alternatively, perhaps there is a trend in Rockland County that DSS does not pursue anything.

If the chances of contribution pursuit are low, then it may not be worth converting.

6. How much over the CSRA is the community spouse going to be?

(This question also ties into risk tolerance and knowledge of your local DSS.) If the community spouse will only be $50,000 over the CSRA, perhaps there is a significantly smaller likelihood that the DSS may request a con-

tribution. If so, perhaps converting the excess resource into an income stream is not the ideal solution.

7. What are the transaction costs involved in converting the excess resources into an income stream?

In addition to increased legal fees and possible accountant costs for allocating the income and interest earned on the income, do you have to pay for the creation of the note or the annuity?

8. What types of investments are being exchanged/liquidated to get the fixed income?

Will the community spouse face capital gains taxes on the liquidation of the resources in order to convert it into an income stream? If so, are the taxes due larger or smaller than a possible contribution claim?

If the assets to be sold/liquidated are all stocks with a low basis, then it may not be worth converting. If the assets are just cash sitting in a bank account and the client is looking for something to do with the funds anyway, then this may be a different conversation to have.

In sum, although the concept of converting excess resources into an income stream is an excellent yet complex tool, it is important to consider the above factors prior to utilizing this tool as in some cases, this may not be the ideal tool to accomplish all of the client's goals.

Endnotes

1. *See* New York Social Services Law ("NY SSL") §366.5(e)(4)(ii)(A).
2. *See* NY SSL §366.3(a).
3. The implied contract is only created if the spouse has sufficient income and resources at the time that Medicaid is provided. *See Commissioner of the Dep't of Soc. Servs. v. Spellman*, 672 N.Y.S.2d 298 (1st Dept. 1998).
4. *See* NY SSL §366.3(a).
5. *See* Medicaid Reference Guide at p. 277.
6. *See* NY SSL §366-c.2(h); 18 NYCRR 360-4.10(a)(8).
7. *See* NY SSL §366-c.2(d); 18 NYCRR 360-4.10(a)(4)(ii).
8. *Commr. of the Dept. of Social Servs. of the City of N.Y. v Scola*, 2011 NY Slip Op. 33019[U] [Sup Ct., NY County 2011].
9. 18 NYCRR 360-4.10(b)(5).
10. NY Social Services law 366-c.8(b) and NY Social Services Law 366-c.8(c); 18 NYCRR 360-4.10(b)(6) and 18 NYCRR 360-4.10(c)(7).
11. GIS 15 MA/21.
12. NY Social Services Law 366.5(e)(3)(iii); 06 OMM/ADM-5, GIS 06 MA/016 and Medicaid Reference Guide Page 334 (updated June 2010).
13. 18 NYCRR 366.5(e)(3)(i); *see also* 06 OMM/ADM-5, GIS 06 MA/016, and Medicaid Reference Guide pages 452-54 (updated January 2011).
14. 1-7 Bender's New York Elder Law § 7.03(2) (2015).
15. 18 NYCRR 360-4.10(b)(4); Medicaid Reference Guide page 276 (updated November 2007).
16. Medicaid Reference Guide at 277 (November 2007).
17. NY SSL 366.5(e)(3)(iii); 06 OMM/ADM-5, GIS 06 MA/016 and Medicaid Reference Guide, Page 334 (updated June 2010).
18. The longer the term of the note, the lower the income. At the end of the day you are tying up your client's funds. The question is—for how long?

Regina Kiperman is a Partner and Naomi Levin is an Associate with Grimaldi & Yeung, LLP. Regina focuses on Probate and Estate Administration, Estate Litigation, Elder Law (including guardianship and Medicaid planning), and Estate Planning. Naomi focuses on Elder Law, Estate Planning, and Guardianship.