



## Current Concerns with IIOT's and Medicaid Planning

By: Brian Mahoney, Esq.



In the January 2009 issue of *The WealthCounsel Quarterly*, I discussed some of the clauses that can make an Irrevocable Income Only Trust (IIOT) more flexible in the event Trust home realty were to be sold or in the event the Grantor needed to change the Trustee or Beneficiaries.

IIOT's have been utilized in attempts to ensure a trust owned asset is non-countable in the event a nursing home is required five years and a day after the asset is transferred into the IIOT. If you do not make the 5 years there would be a problem and now if the Nursing Home cannot be paid there may be a civil Fraudulent Transfer complaint.

There are many mechanisms and important clauses that often make up an IIOT, but when are they appropriate to be recommended to a Client in today's political and economic climate? Irrevocable means it can never be changed, but the Law and facts do change. So we need a document that must be solid enough to pass Medicaid scrutiny, but somewhat flexible as needs change. I am not so sure that can be achieved today with any certainty.

I now send a prospective Client a letter in advance of the initial meeting in memo form, detailing the pros and cons of an IIOT. I later ask them to sign that memo at the signing ceremony, before we execute an IIOT to discuss, for one last time, the issues involved.

Is an IIOT good for everyone? Certainly not. Saving a legacy to pass onto Family is an admirable goal. But citizens today are living longer and longer and can outlive their assets. Goal One for any Client should be to talk to their trusted C. P. A. or Financial Planner to determine if they might ever need to sell assets to live off the sales proceeds.

Questions that need to be addressed include:

- What is income expected to be? (Underestimate projected income.)

- What are expenses expected to be? (Overestimate projected expenses.)
- Is there adequate Health Insurance?
- Medicare coverage?
- Long Term Care Insurance?

If the Client might need to someday assets to live off the sales proceeds, then this type of trust is clearly not for them.

We should also warn Clients that no financing of any type can ever be obtained for realty in an IIOT. No reverse mortgages can be obtained either. Recently clients of mine had difficulty obtaining homeowners insurance on a beach home in Maine they had deeded into an IIOT.

A home in an IIOT can be sold and another purchased in its place and of course we can draft it as a Grantor Trust so that we could make use of the 121 exemption from capital gains. But what if the Grantor has no money to pay for any gain that might remain over and above the exemption? It can happen. What if the adult child beneficiaries do not have liquid funds to pay the tax for the Grantor/Parent? If the Trust paid the tax due Medicaid would count the trust corpus.

How would we make it a Grantor Trust? Would we use a testamentary and lifetime power to appoint the contingent beneficiaries? That is always a good way for the Grantor to keep the adult children in line. It is also an avenue of attack by the government now regarding any lifetime powers over principal and that can make the trust corpus vulnerable.

If you grant the right to live in the home within the IIOT then we may now see government attacks that such a right constitutes "use of Principal." I strongly disagree. If the right to reside in trust owned realty is not in the IIOT, then the Grantor has to rely on the discretion of the Trustee. There seems to be no prohibition on a Grantor being a trustee, but will that be helpful if the IIOT is attacked?

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Should we allow for removal of a Trustee by the Grantor if the Grantor is not named as the Trustee? Will that make it amenable to attack?

The case of Doherty v. the Director of the Office of Medicaid is going to the Appeals Court in Massachusetts. Issues surrounding this Trust's provisions are: 1. Allowing the Grantor to reside in trust owned realty for life. 2. The Grantor's limited power of appointment of trust principal to her family but not to her, her estate, her creditors, nor to her estate's creditors, and 3. The Grantor's right also to veto a sale of trust realty. This involves a poorly drafted trust that hopefully will not lead to bad caselaw. This IOT also allowed the Trustee to adjust, apportion and allocate any receipt or gain, between principal and income, which allowed the Government yet another aspect to attack. In many trusts I have seen provisions allowing a trustee to terminate the trust if it is economically inadvisable to continue, drafted perhaps in the event the corpus could become virtually exhausted and so small, that it could be economically wasteful to continue the trust. This provision, the government asserts, renders the trust corpus countable and makes this IOT not irrevocable. We await the Court's ruling and dicta, if any in the decision.

One's age and health are also important considerations in determining whether to execute an IOT. If one did not make the five (5) year look back period then the home in the trust would be considered a countable asset which would make one ineligible for Medicaid. "Trap doors," or so-called "escape hatches," used to appoint principal to a group of persons perhaps consisting of adult children are often used in IOT's. If an Attorney were to orally advise a Client that a trap door could be used to funnel trust principal to an adult child who could then pay for the Grantor parent's nursing home care until the look back period is attained, is he/she engaging in fraud, or just good lawyering? I submit it clearly is the later. Will Courts rule those escape hatches are equal to control of principal by the Grantor?

Will Medicaid continue to attack these types of Clauses as the economy lags, budget crises prevail and deficits in Government continue? Yes. The Courts see themselves as Guardians of the State's coffers. Medicaid was designed

to take care of only the poor and the needy. I have represented many of the "greatest generation," and believe they should be able to pass their home onto their children and also obtain Medicaid sponsored Nursing Home care, but that is not the government's view.

I now believe we will see an increase in Nursing Homes bringing Fraudulent Transfer cases where there have been spend downs and transfers and when a gap between private pay and Medicaid occurs because of impermissible transfers and resulting Penalty periods. I defended one such case a few years ago and was successful. My Client prevailed because they followed the law re allowable spend down and transfers, but will that continue? A sympathetic trial Court Judge will be taken to an Appellate Division now by the NH in many instances. Will the Courts rule that following traditional methods of Medicaid Planning and making permissible transfers allowable under Federal and State Law will no longer be permitted if it rendered the Grantor insolvent? No intent is usually required under most state's fraudulent transfer acts.

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