What you don’t know about gifting, the annual gift exclusion, and Medicaid.

By Mary Ellis Patton
Edited by Carolyn L. Kenton

Are you afraid to give a gift of more than $14,000 in any one year because you will have to pay taxes? Are you confident that making the $14,000 annual gift will keep you Medicaid complaint?

If you ask an adult American how much they can give away each year without paying taxes, most will automatically respond, “$14,000.” It has become almost a part of the American DNA. Unfortunately, most people misunderstand the rule.

The Gift Tax Rule

The annual gift tax exclusion is really a reporting rule. Any gift over $14,000 must be reported on a federal gift tax return, IRS form 709. This does not mean that you pay tax on it. Gifts reported on Form 709 count towards the lifetime federal gift tax exclusion (which in 2016 is $5.45 million per person). No tax is owed until the gift-giver exceeds total gifts of $5.45 million.

Annual gift-givers can give to as many people as they wish. The $14,000 figure applies to gifts made to each individual person – not the total of the gifts made in a single year.

Married couples can double the gift amount without being required to report. Yes, a married couple, can for example, give $28,000 to each of their children (and their spouses) without having to report the gift.

With proper planning, a married couple can gift $10.9 million, plus as many annual gifts as they choose, without paying gift tax.

Why the Gift Tax Rule Doesn’t Matter

With the gift tax exclusion being at $5.45 million, few estates are paying federal gift tax. In fact, 99.8% of estates do not owe gift tax.1 That means that only the richest 0.2% of Americans are actually affected by this rule.

If you want to give a large gift to a child or another loved one, there is likely nothing holding you back. Most Americans will simply not gift more than $5.45 million in their lifetime. There is no reason to fear, give your gift, fill out your Form 709, and enjoy.

Gifting and Medicaid

The Gift Tax Rule is exclusively a tax rule. It is not a Medicaid rule. Medicaid does not take the gift tax rule into consideration and will penalize gifts made in the five years prior to the Medicaid application.
Medicaid considers any gifts made in the five years prior to an application for Medicaid financial assistance to be made in contemplation of that assistance. Thus, Medicaid will assign a penalty period for gifts made within the five year “lookback” which starts when the client is “otherwise eligible” (eligible except for the gift) and has applied at the Medicaid office for assistance. Medicaid calculates a penalty which is a period of time of ineligibility for financial assistance.

For clients who have done no planning and now have a family member residing in a nursing home, lifetime gifting can still be beneficial as the family may be able to preserve up to half of the value of the gift by “curing” the gift in a “give-and-give-back” or “half-a-loaf” strategy. This involves returning a portion of the gift in a prescribed manner and reapplying for Medicaid in a timely way. This strategy should only be done with an attorney’s help and supervision.

**Possible Tax Concerns for Gift Recipients**

While the gift-giver will likely not have tax consequences for giving the gift and the gift recipient will not pay income tax on the gift, the recipient still needs to be aware of potential capital gains income taxes when he wishes to liquidate the asset. Under federal law, the new owner of the gifted asset retains the cost basis (often the acquisition cost) of the gift giver. Thus, if the gift giver’s home is the subject of the gift and the gift giver purchased the home for 25 percent of its current value, the gift-recipient owner, when selling the house, will incur a capital gain of 75 percent of the sale price. To avoid this result, the home can be sold by the gift giver using his $250,000 capital gains tax exclusion and gift the cash.

**Conclusion**

If you are thinking about using a gifting strategy in conjunction with your estate plans, you should contact an elder law attorney. Gifting can be a wonderful planning technique if you are able to weigh the benefits and consequences.

©2016 by Bluegrass Elderlaw, PLLC, 120 N Mill Street, Ste 201, Lexington, KY 40507, www.bgelderlaw.com

---

ESTATE PLANNING
GLOSSARY OF TERMS

BENEFICIARY - One for whose benefit the will and/or living trust is created.

CONSERVATOR - A person who has the legal duty to care for and maintain the property of an incapacitated adult.

ESTATE TAXES - The taxes imposed by the federal government on the transfer of assets at death. Estate taxes are generally paid by the personal representative of the probate estate or the trustee of a living trust.

EXECUTOR/PERSNL REPRESENTATIVE - The person or institution who is appointed by the testator or testatrix in his or her will to manage the funds and property of the estate after death and distribute them to the designated beneficiaries. The executor functions under the jurisdiction of the probate court.

FIDUCIARY - The statutory obligation to manage assets in the same way a prudent person would manage his own assets.

GUARDIAN - A person who has the legal duty to care for and maintain the person and/or property of an incapacitated adult or an unmarried minor child.

HEIR - A person who inherits property (according to state law scheme of distribution) from a person who dies intestate.

INHERITANCE TAX - The taxes imposed by the State of Kentucky on gifts to others than issue.

INTESTATE - A situation where a person dies without leaving a valid will.

ISSUE - Lineal descendants of all degrees (e.g., children, grandchildren, great-grandchildren, etc.).

JOINT TENANCY IN COMMON - A co-ownership of property by two or more parties in which each owns an undivided interest that passes under a will or by intestacy.

JOINT TENANCY WROS - A co-ownership of property by two or more parties in which each owns an undivided interest that passes to the other co-owners on his or her death (known as the "right of survivorship").

LIFE TENANT - A trust or estate beneficiary whose interest consists solely for the use of, and income flow from, the trust funds during his lifetime.
LIVING TRUST - A legal entity established by means of a written trust agreement during the lifetime of the creator of the trust. The terms of the trust agreement govern the operation of the trust funds. The trust becomes irrevocable upon death of the trust creator.

PROBATE - The legal proceeding by which the probate court is given full jurisdiction over the assets of the decedent. Probate starts with the opening of the estate by filing the decedent’s will or intestate petition with the probate court, and ends after all taxes and debts of the decedent have been paid, the assets accounted for and distributed in accordance with the terms of the decedent’s will or the law. Probate lasts for six months to permit creditors to submit their claims but there is no maximum term depending on the status of the property transferred and the debts of the decedent. Depending on the circumstances of the estate, all estate funds do not necessarily have to be sequestered for the full six months.

REVOCABLE LIVING TRUST - A living trust governed by a trust agreement whose terms may be amended, modified, or otherwise revoked by the trustor during his lifetime. The same thing as a Living Trust or an Inter Vivos Trust.

TESTATOR - (If female, TESTATRIX) - A person who makes a will.

TRUSTEE - The person or institution who is responsible for holding, managing, and distributing money and other property contributed to the living trust for the exclusive use and benefit of the beneficiaries.

TRUSTOR/SETTLOR/GRANTOR - Parties who establish a trust by transferring property to a trustee to be managed for the benefit of another.
What You Need to Know About
Powers-of-Attorney

Most adults should have the following estate planning items: (1) A list of assets, accounts, insurance policies, and funeral instructions; (2) Living Will (also called Final Directives); (3) a Last Will and Testament; and (4) Powers-of-Attorney that cover Health Care, Legal, and Financial matters.

While all of these documents are important, the only legal documents that operate during your lifetime are your Powers-of-Attorney (both Healthcare and Legal/Financial). These documents, when drafted correctly, can aid in preparing for end-of-life matters and managing your day-to-day living needs as you age. Therefore, they are the most important legal documents for you to have during your life. These documents should be carefully drafted to make sure they cover all areas of your life.

Our firm drafts these documents in two parts: one POA addresses Health Care and a second one covers legal and financial affairs. This gives individuals more latitude in choosing their Attorneys-in-Fact (also called "agent").

Power of Attorney – Financial

1. What is it? A “POA” is a written document where one person (the “principal”) appoints another person (agent or Attorney-in-Fact) to act with authority on their behalf to perform acts specified in the document.

2. Modern times call for Powers of Attorney with robust powers to provide for legal and financial affairs even when the principal has become incapacitated.

3. Grants of Specific Powers
   a. Real Estate – If the POA grants the ability to transfer real estate, the document should be filed with County Clerk.
   b. Gifting – A gifting provision will enable families and their attorney to undertake appropriate Medicaid asset preservation planning. Your POA should specify that gifts of any amount may be made to your spouse, children, or grandchildren or other designated individual(s).

Power of Attorney – Health Care

1. This document grants specific powers to access your health care information. This can include physical and mental health records. Additionally, this document gives your agent the power to make medical decisions on your behalf.

2. Modern Health Care POAs should contain required HIPPA waivers.

Bluegrass Elderlaw, PLLC
WWW.BGELDERLAW.COM  ♦  859.281.0048
Choosing Your Attorney-in-Fact or Agent

The choice of your Attorney-in-Fact is as important as the language contained in the documents. Your Attorney-in-Fact will have power to do a great many things. If you are hesitant about naming someone, they may not be the best choice. Trust is the most important factor. The wise choice is a stable, financially responsible person on good terms with the other family members. You should avoid naming someone who may have substance abuse, mental illness, financial problems (debt), gambling or addiction problems, be a dependent person or a controlling person, a child in conflict with his or her siblings, or someone going through a divorce or bankruptcy.

The Agent’s Role

When a loved one names you to be their attorney-in-fact or agent, you must follow the instructions contained in the authorizing document. Most importantly, a POA is not a document that can be used to impose your will on the principal. The principal still has the ability to make decisions on his own. (You cannot “get power of attorney over” someone.) Only a guardianship can take those fundamental rights away.

The POA’s Effective Date. POAs take effect in one of two ways. First, they take effect as soon as the principal signs it. Or, the POA takes effect only when a certain event takes place. Usually this “event” is the principal’s incapacity as determined by one or two licensed physicians. If the POA is this second type, be aware that it may take significant time to get a physician to give you this determination in writing.

The POA’s End Date. Your duties to the principal end upon his death or his revocation of his POA or your resignation. You must stop using the POA immediately at that time. You have the right to resign as agent. The POA may specify the requirements for doing so.

Four Big Responsibilities:

1. Act only in the best interest of the principal. You need to avoid conflicts of interest. Make decisions based upon what the principal desires or would want done if competent.
2. Manage his/her money responsibly. You should make informed and careful decisions. This may require you to get professional assistance from an attorney, accountant, or financial advisor.
3. Do not mingle their finances with your own. Use their money for their needs and benefits only. This might be slightly different if the principal is your spouse.
4. Keep accurate records of their finances – income and expenditures.

* Failure to do these could result in legal consequences

If you have questions about your Power-of-Attorney document or your role when named as an agent in a Power-of-Attorney, you should consult an Elder Law attorney. These are powerful legal documents and when correctly drafted and used appropriately, they can be a formidable and effective estate planning tool.

Bluegrass Elderlaw, PLLC
WWW.BGEELDERLAW.COM ♦ 859.281.0048
Many married couples are unaware of an important element of asset preservation when faced with long term care expenses -- the Medicaid Resource Assessment. A portion of the Medicaid rules is designed to protect the community spouse (spouse at home) from impoverishment and unnecessary dissipation of family assets. Only the institutionalized spouse (spouse in a facility) is required to have assets of $2,000 or less and a pre-paid funeral.

The inspiration for this article came from a very recent trip to the Medicaid office by one of our staff members. She was waiting to speak to a caseworker and began to chat with a parents had spent down all of their assets, more than $100,000, in order to reach a balance of $2,000 so his father could be Medicaid eligible. She came to my office afterwards, heartbroken for the man and his family. They never knew about or obtained a Resource Assessment from the Medicaid office.

The failure to have a proper Resource Assessment in a timely manner can cost couples thousands and even hundreds of thousands of dollars. The community spouse is entitled to
keep a portion of the family assets and the Medicaid office establishes that amount at the
time of the Resource Assessment. During the Resource Assessment, the caseworker will
look at the countable assets belonging to the couple and allocate them between
them. Depending on the amount of the countable resources, the community spouse can
keep half the amount (or a minimum of $23,844 up to $119,220). At that time the
caseworker will determine the amount of the spenddown (if one is necessary) in order to
qualify for Medicaid.

The Resource Assessment operates as a snapshot of the assets owned by a married
couple. A delay in obtaining the assessment will reduce the amount of assets available to
be set aside to the community spouse. It is better to obtain the Resource Assessment
sooner rather than later (within the first couple of months of institutional placement) when
assets are higher rather than lower – yes, you want to walk into the Medicaid office for
your Resource Assessment owning more assets than less! The patient usually is not
eligible for Medicaid at the time of the assessment which makes the assessment even more
important. It may not make sense until you see how it works.

Example:

Judy and John, a long-time married couple, were devastated when Judy had to be placed in
the nearby skilled nursing facility. Judy and John were both well-educated individuals and
knew that for Judy to be eligible for Medicaid, they would have to spend down their
resources. John read articles in magazines and the internet about Medicaid. He knew Judy
could only have $2,000 in assets. Both of them have retirement accounts, they own their
home and one car, and John has $80,000 in a non-retirement investment account.

The Wrong Way for Judy to qualify is to spend down all their assets until they have only
$2,000 in family assets. While she will certainly qualify when the application is made, John
will be without assets that he could have retained.

The Right Way for Judy to qualify is to get a Resource Assessment as soon as Judy goes to
the nursing home. The Medicaid caseworker will tally up the countable assets, which, in
this case, is only the $80,000 account (because, in the state of Kentucky, the retirement
accounts are exempt assets) and then divide the assets in half. Judy gets $40,000 in her
“bucket.” John gets $40,000 in his “bucket.” The home and the car are exempt for the community spouse. John and Judy’s spend-down amount is $38,000; they will need to spend the funds in Judy’s “bucket” until her assets are only $2,000. These monies can be spent on either of them. John could buy a new car, pay down the mortgage, remodel the home, buy special things for his wife like a new TV or clothing. After Judy’s bucket is at $2,000 or less, she can apply for Medicaid and will be eligible.

**Tips for your Resource Assessment:**

1. Clean up extraneous bank accounts. Think about closing or consolidating accounts you no longer use.

2. After a nursing home placement, the community spouse’s income should be deposited into a separate checking accounts in his or her name alone. The institutionalized spouse’s income should continue to be deposited into a checking account owned jointly with the community spouse. The joint account should be used for the institutionalized spouse alone. Any allocation of income from the institutionalized spouse to the community spouse should be transferred to the community spouse’s account before being spent for the community spouse.

3. After the Resource Assessment, think about moving the spend-down funds to a separate account and spending from that account. When the account has been depleted, it is time to make the Medicaid application if the patient is in a Medicaid designated bed.

4. Keep all your bank records and purchase receipts and be prepared to trace all your fund transfers.

5. The Medicaid worker should give you or your representative the Resource Assessment with the spend-down amount. (This form is PA-22.) *Do not leave the office without it* because the Medicaid office will not retain a copy for you.

*Interactions with the Medicaid Office can be overwhelming. If you want to know more or need help, contact a qualified elder law attorney.*