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NJ ELDER AND DISABILITY LAW UPDATE 2008

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Presented for:
The Other Big 8
I. FEDERAL ELDER AND DISABILITY LAW UPDATE

A. Medicare Changes

1. Hospice Services-Effective January 1, 2008, hospice providers have the option to report more detailed information on hospice claims and the location where differing levels of hospice care are delivered. As of July 1, 2008 such reporting is mandatory under Medicare Transmittal 1397.

Unlike other types of claims for which Medicare imposed on providers more complex reporting and payment methods, there have been no significant changes for hospice claims since the inception of those services. Since 1983, hospice care providers have only been required to report the number of days at each of the four hospice levels of care and details as to procedures performed by a Medicare beneficiary’s attending physician if the physician was a hospice employee. Now hospices will be required to report (i) the number of services and visits provided by nurses, home health aides, social workers, physicians and nurse practitioners by category (items and services within the visit will no longer be separately counted); and (ii) the location where the care was provided (including separate service codes for Medicare covered skilled nursing facility stays and non Medicare covered skilled nursing facility stays). A service or visit consists of direct care to the beneficiary that is medically reasonable and necessary. A claim for service does not include an entry in the medical record without direct care or rounds in a facility.

Further, certain principal diagnoses, such as history of stroke, positive tuberculin test, physical therapy, palliative care and radiation therapy, will no longer be accepted as fulfilling the necessary “terminal diagnosis” requirement for hospice care. The terminal diagnosis requirement is met by a doctor certifying the patient is terminally ill and has six months or less to live if the disease runs its normal course.
As a result of these changes, it will likely be more difficult for clients to obtain Medicare coverage for hospice care.

B. **INCOME TAX UPDATE**

1. **I.R.C. SECTION 121**-The “Mortgage Forgiveness Debt Relief Act of 2007” added subsection (b)(4) to I.R.C. §121 to provide a special rule for certain sales by surviving spouses made after December 31, 2007. Specifically, a property sold by an unmarried surviving spouse is eligible for capital gain exclusion of up to $500,000 (i) if the sale occurs within two years of the date of the first spouse’s death; and (ii) if at the time of the first spouse’s death the requirements of IRC §121(b)(2)(A) are met, that is:

(a) either spouse owned the property for an aggregate period of two of the previous five years;

(b) both spouses used the property for an aggregate period of two of the previous five years (See I.R.C. §121(d)(7) for special rules for nursing home residents); and

(c) neither spouse used an I.R.C. §121 exclusion during the previous two year period.

Previously, property sold by a surviving spouse was only eligible for the $500,000 capital gain exclusion during the year that a joint return was filed, effectively limiting such sale to the year of the death of the first spouse.

2. **PLR 2007-29019** addresses the deductibility of tuition for a medically handicapped dependent child as a medical care expense under I.R.C. §213(a). The child was developmentally disabled and a neuropsychological report stated she needed a support program such as offered by the school. The school provided tutoring and specialized social, academic and independent living skill development to enable its students to succeed in neighboring colleges and technical schools. It did not provide college courses or living facilities and the student’s tuition at the neighboring school was paid directly to those institutions.

The IRS ruled that the school was a “special school” within the mean of Reg. Sec. 1.213-1(e)(1)(v)(a) because its program was designed to enable the child “to compensate for and overcome her diagnosed medical conditions” and the tuition paid to the school could therefore be deducted as a medical expense under I.R.C. §213.

3. **THE TEMPORARY TAX RELIEF ACT OF 2007 (“TTRA”)** proposes to extend the charitable tax provisions of the Pension Protection
Act of 2006 ("PPA") which expired on December 31, 2007. *Inter alia*, the TTRA extends:

(a) the IRA charitable rollover-The PPA provided that up to $100,000 per year may be excluded from income for qualified charitable rollovers from a traditional IRA or Roth IRA to public charity or conduit private foundation if (i) the individual is 70½ by distribution date; (ii) the distribution was made before December 31, 2007; and (iii) the distribution was be made directly to a qualified charity. Qualified charities include community foundations, designated funds and endowment funds unless the donor has input over distributions. Private foundations, partial interest gifts (e.g. CRTs and CLTs) and donor advised funds are excluded;

(b) food inventory gifts-individuals or C corporations can receive an enhanced deduction for gifts of “apparently wholesome food” to charities;

(c) computer gifts—C corporations can receive an enhanced decution for gifts of computers to educational organizations or libraries;

(d) qualified conservation contributions will receive a deduction of up to 50% of adjusted gross income (previously 30%);

(e) shareholders will be able to deduct the fair market value of gifts of appreciated property made by Subchapter S corporations directly to charities and the shareholders’ outside basis is reduced only by the S corporation’s inside basis.

The TTRA (H.R. 3996) was passed by the House of Representatives in November 2007 and was placed on the Senate calendar but has not been passed by the Senate as yet. On February 4, 2008, President Bush transmitted the proposed federal budget for 2009 to Congress, which included the above-listed charitable tax provisions.


On January 16, 2008 in a unanimous decision, the Supreme Court held that income tax deductibility of investment advisory fees paid by a trust were subject to the 2% floor under IRC §67(e)(1). The trustee argued that the issue should be whether an expense is the result of the asset being held in trust. The Court decided that such an approach would result in every trust expense being fully deductible and the exception to the 2% rule would swallow the rule. The Court stated that the only costs not subject to the 2% floor and those that would not commonly or customarily be incurred by individuals. The fully deductible trust related expenses
must be unique to the administration of a trust. The trustee further argued that the investment advisory fees should be fully deductible because he incurred them due to his fiduciary obligation of prudent investment. The Court held that the prudent investor standard does not only refer to a prudent trustee but also to a prudent individual investor and therefore it cannot be said that the fees were incurred because the investments were in a trust.

On February 27, 2008, IRS issued Notice 2008-32 to provide interim guidance on the treatment of investment advisory costs, which are subject to the 2% floor under I.R.C. §67(a) that are (i) “bundled” together with commission or fee paid to a fiduciary and (ii) are incurred by a nongrantor trust or estate. The Notice allows taxpayers to deduct the full amount of the bundled fees without regard to the 2-percent floor for any taxable year before January 1, 2008. Other payments to third parties for expenses subject to the 2-percent floor are readily identifiable and must be treated separately from the bundled fee. Final regulations on this issue are expected to contain one or more safe harbors for the allocation of fees and expenses between those costs that are subject to the 2-percent floor and those that are not for taxable years after January 1, 2008.

C. CMS “NEVER ENDING PENALTY PERIOD”

The Centers for Medicare & Medicaid Services (“CMS”) state that the Deficit Reduction Act of 2005 (Pub. L. No. 109-171, 120 Stat. 4, 151) (“DRA”) does not permit a person to receive benefits under a Medicaid waiver program if there has been a transfer of assets within sixty months of the Medicaid application. New Jersey has informally adopted CMS’ position on this issue. This position, dubbed the “Never Ending Penalty Period,” is based on the following:

Among the many changes made to federal Medicaid law by the DRA were changes to the treatment of asset transfers made on or after Feb. 8, 2006 by Medicaid applicants. Specifically, (i) Medicaid’s “look-back” period for all asset transfers is extended from thirty-six to sixty months. 42 U.S.C. § 1396p(c)(1)(B) and (ii) the start of the penalty period for assets transferred on or after the date of the enactment of the DRA is changed from the date of transfer to the date when the individual transferring the assets is eligible for medical assistance under the State plan and would otherwise be receiving an institutional level care described in subparagraph (C) based on an approved application for such care but for the application of the penalty period. 42 U.S.C. § 1396p(c)(1)(D)(ii). Subparagraph (C) describes the services as either (i) nursing facility services; (ii) a level of care in any institution equivalent to that of nursing facility services; or (iii) home or community-based services furnished under a waiver granted under 42 U.S.C. § 1396n(c)or (d).
The circuitous argument for the Never Ending Penalty Period is that the penalty period for an individual who has made a transfer of assets within 60 months of applying for benefits under a home or community-based program cannot start until the applicant is receiving services under the Medicaid program. Problematic is that the individual cannot receive waiver services under the Medicaid program because, under New Jersey’s Medicaid regulations, a medical assessment will not be completed and no application for such care approved until financial eligibility is determined; however, this will never occur during the look-back period because of the ineligibility period triggered by the asset transfer. Perhaps it is more properly referred to as the “Never Beginning Penalty Period.”

In contrast, New Jersey statute provides that if an applicant for home or community-based Medicaid services under 42 U.S.C. § 1396n(c) disposed of resources or income for less than fair market value within 36 months (or 60 months in the case of a trust) shall be ineligible for assistance for those services. The period of the ineligibility shall be the number of months resulting from dividing the uncompensated value of the transferred resources or income by the average monthly private payment rate for nursing facility services in the State as determined annually by the commissioner (currently $6,655). N.J.S.A. §30:4D-3i(15)(b).

See CMS Powerpoint Presentation provided courtesy of John Callinan, Esq. attached as Exhibit A.

II. NEW JERSEY AND RELATED STATE ELDER AND DISABILITY LAW UPDATE

A. MEDICAID PLANNING TECHNIQUES

1. COMMERCIAL ANNUITIES


   A community spouse husband purchased an irrevocable annuity with marital assets. The beneficiaries of the annuity on his death were his children. The subsequent application for nursing home benefits for his institutionalized wife was denied by Medicaid based on a finding that the annuity was an available resource. The Medicaid denial was affirmed by an administrative law judge who determined that (i) under the terms of the annuity the community spouse could sell his right to the income stream; (ii) the present value of the income stream exceeded the community spouse resource limit; and (iii) the community spouse was not the only beneficiary of the annuity which had the additional purposes of providing a “tax-free, probate-free vehicle” for the transfer of wealth to his
children and to qualify the institutional spouse for Medicaid benefits. On appeal, the court held that income and resources must be treated separately pursuant to federal law. The annuity income available to the community spouse cannot, therefore, be deemed a resource available to the institutionalized spouse.


A nursing home resident was ineligible for Medicaid benefits as a result of his wife’s purchase of a single premium immediate irrevocable annuity. The annuity was actuarially sound, i.e. monthly income payments would be made to the community spouse for eight years and her life expectancy was 10.24 years at the time the annuity was purchased. By its terms, the annuity had no cash surrender value. Medicaid claimed that the annuity had a market value of $185,000, which exceeded the permissible community spouse resource allowance (CSRA). On appeal, the court held that the purchase of an actuarially sound irrevocable commercial annuity by a community spouse for her sole benefit did not count as a resource for Medicaid eligibility purposes. In addition the income from the annuity is not considered in determining Medicaid eligibility. Income of a community spouse is unavailable to an institutionalized spouse. 42 U.S.C.A. § 1396r-5(b)(1).

Oral argument on the appeal of this case is scheduled for March 4, 2008 in the Third Circuit before Chief Judge Scirica and Judges Roth and Fisher.

2. PROMISSORY NOTES

The DRA mandates that funds loaned in exchange for a promissory note or mortgage be considered a transfer of assets unless the repayment terms are actuarially sound; provide for equal payments and prohibit the cancellation of the balance upon the death of the lender. 42 U.S.C. §1396p(c)(1)(I).

Although the loan in exchange for the promissory note may not be deemed to be a transfer of assets, New Jersey may still consider the note as a countable asset unless it can be proved that there is no secondary market where the note can be sold. Companies like J.G. Wentworth have provided letters for use in the Medicaid application indicating that they are not willing to purchase the promissory note.

A client may consider loaning money to their children in exchange for a promissory note. This may be done in conjunction with or as an alternative to transferring assets.
As an example, if a community spouse, gave $1,000,000 to her children in exchange for a note, the term of the note must be the community spouse’s actuarial life expectancy under the Social Security table. For example, if the community spouse was 76 years old having a life expectancy of 11.4 years, and assuming an interest rate of 3.6% (the current IRS applicable rate) the children must make equal monthly payments to the community spouse of approximately $10,572.37. These payments will be a stream of income to the community spouse. A community spouse’s income will not be considered when determining an institutionalized spouse’s Medicaid eligibility. Consider the same transaction, but instead of the community spouse loaning the funds to the children in exchange for a promissory note, a Medicaid applicant makes the loan. The repayments would be counted as income to the applicant and make Medicaid unavailable to the applicant because the applicant’s income would likely exceed the cost of his or care.

It appears that currently at least some counties are sending all promissory notes to Trenton for review. Since there is no transfer penalty for a promissory note meeting the standards discussed in the previous paragraphs, the client can utilize this as an “11th hour” planning technique and wait until Medicaid eligibility is imminent before exchanging any assets for a promissory note.

3. **INCOME ONLY AND FAMILY TRUSTS**

(a) Background

“Income Only Trusts” (IOTs) or “Family Trusts” (FTs) gained favor when COBRA 1985 legislated out of existence certain discretionary trusts then commonly used, denoting them as “Medicaid Qualifying Trusts (MQTs)”. MQTs were inter-vivos trusts established by an individual Medicaid applicant or the individual’s spouse under which the individual or individual’s spouse was the beneficiary of all or part of the payments from the trust as determined in the absolute discretion of the trustees. Specifically, 42 U.S.C. 1396a(k)(2) [now repealed], deemed the assets of such irrevocable trusts to be available resources when determining the Medicaid eligibility of the individual or individual’s spouse.

From August 10, 1993 until February 8, 2006, the effective date of the DRA, the period of time for reporting any transfers when applying for Medicaid benefits (the “look-back period”) for outright transfers was the 36 months immediately prior to the date of the Medicaid application, and for transfers involving a trust, the
look-back period was 60 months. Transfers within the look-back period are penalized by a period of Medicaid ineligibility calculated by dividing the value of the transfer by the regional nursing home rate to obtain the number of months of ineligibility, or penalty period. 42 U.S.C. § 1396p(c)(1)(B)(i); N.J.S.A. § 30:4D-3(i)(15)(b); N.J.A.C. § 10:71-4.10(b). During this time, elder and disability law practitioners, when counseling clients regarding asset transfers, had to balance (i) the extended look-back period triggered by the implementation of IOTs and FTs required to obtain certain tax and other planning benefits with (ii) the shorter look-back period triggered by outright transfers despite concerns regarding loss of client control and creditors’ claims.

The DRA extended the look-back period for transfers made on or after the DRA enactment date to 60 months, regardless of whether a trust is involved. This extension of the look-back period for all transfers allowed practitioners and clients again to consider in almost every circumstance using an IOT or FT as an asset divestment option on a “level playing field” from a look-back perspective despite continuing concern about possible New Jersey estate recovery issues.

(b) Description: An irrevocable trust created by a Medicaid applicant or the applicant’s spouse (the grantor). During the lifetime of the grantor, income is payable to the grantor or the grantor’s spouse, or payable in the trustee’s discretion to other beneficiaries, and principal is retained or payable in the trustee’s discretion to beneficiaries other than the grantor or the grantor’s spouse. At the death of the grantor, the trust may continue with income payable to the grantor’s spouse and principal retained or paid to beneficiaries other the grantor’s spouse, or the trust terminates and is paid to remainder beneficiaries.

The funding of an IOT or FT is deemed an uncompensated transfer for Medicaid purposes and will trigger a look-back period and if the Medicaid application is filed within the look-back period, will result in a period of ineligibility. Payouts from the trust to beneficiaries other than the grantor or the grantor’s spouse will not be deemed uncompensated transfers.

(c) Benefits

i. The trust assets are considered unavailable for Medicaid purposes.

ii. If properly structured will be treated as a “grantor trust” under I.R.C. §673-677.
(1) income taxed at the grantor’s individual rates which are usually less compressed than the trust’s tax rate; and
(2) capital gains, particularly on the sale of the grantor’s residence property, are treated as if owned by the grantor).
(3) Allows the client to retain some control over the disposition of assets at death;
(4) Allows the trust assets to be included in grantor’s estate at death providing opportunity for a basis adjustment to capital assets; and
(5) Allows the trust assets to be protected from creditor claims of the trust beneficiaries except to the extent of grantor’s retained interest

(d) Additional New Jersey Considerations

i. “Trust Buster” statute: invalidates a trust provision that prohibits the trustee from making distributions that would disqualify the disabled individual from receiving Medicaid benefits but seems not to invalidate a trust provision allowing a trustee to exercise sole discretion to make distributions to supplement government benefits. N.J.S.A. §30:4D-6(f); A.M. v. Div. of Med. Assistance & Health Services, Docket No. HMA 8525-05.

ii. J.S. v. Division of Medical Assistance and Health Services, Docket No. HMA-4896-06. J.S. was grantor of an irrevocable Income Only trust; his son was trustee. J.S. had no access or control over principal, but the trust provided that the income be paid annually to J.S. Approximately 2½ months prior to submitting an application for Medicaid benefits, the trustee terminated the trust and retained the assets. DMAHS argued that the entire principal of the trust, as well as the income generated, should be counted as available resources. The applicant grantor argued that since no portion of the trust principal could be used for his benefit from the date it was transferred to the trust, that date should be the starting date for any period of ineligibility. The OAL found that the transfer of assets to the trust was a transfer for less than fair market value, and therefore subject to a 30-month ineligibility period. The income from the trust was an available resource, not subject to a penalty period, but potentially rendering J.S. ineligible for Medicaid benefits. Nevertheless, the OAL
found that the trust was void as a matter of public policy (policy against shielding assets for the purpose of becoming Medicaid eligible) and therefore, the $130,000 is an available resource, and the penalty period did not begin until the date of the Medicaid application.

The Director reversed on that issue (finding that the penalty period began when J.S. gave up his right to principal and transferred the assets to the trust) and remanded the matter to the Middlesex County Board, directing the Board to reconsider the imposition of penalty period on income transfers following trust termination. Id. Final Agency Decision, (March 22, 2007).

iii. IOTs are subject to expanded Medicaid right of recovery at applicant’s death. N.J.A.C. 10:49-14.1.

(e) Issues Surrounding Medicaid Status as a Creditor

i. Medicaid as Creditor

New Jersey’s adoption of expanded estate recovery seems to result in Medicaid's treatment as a “creditor” in this state. New Jersey law has not addressed this specifically. If Medicaid has creditor status then the New Jersey Probate Code particularly the sections that make a trust creator’s reserved trust interest freely alienable to his creditors (N.J.S.A. 3B:11-1) and the priority of claims when estate assets are insufficient to pay all claims in full (N.J.S.A. 3B:22-2) may apply.

In New Jersey, the Appellate Division has held that estate recovery by Medicaid is available against property held in a testamentary elective share trust where the trust was funded with assets transferred from a Medicaid recipient within five years of applying for Medicaid benefits. The court relied on 42 U.S.C.A. § 1396p (b)(4)(B) in finding that the testamentary trust “qualifie[d] as an "arrangement" for the conveyance of the assets of a Medicaid beneficiary” and therefore, remained part of the recipient's estate against which Medicaid could seek recovery of Medicaid benefits. Estate of DeMartino, 373 N.J. Super. at 221.

In New York, Medicaid asserted a claim that the transfer of the marital home to an IOT violated debtor/creditor law. This argument was rejected by the Appellate Division. Accordingly, the Court of Appeals did not
address the debtor/creditor claims, but held that where a wife (community spouse) who asserted spousal refusal but had sufficient income and resources to pay for her institutionalized husband’s costs of care and effectively entered into an implied contract with Medicaid to pay for such care.  I/M/O Tomeck, 2007 NY Slip. Op. 5589, 8 N.Y.3d 724 (June 28, 2007).

ii. New Jersey’s Uniform Fraudulent Transfer Act N.J.S.A. 25:2-20 to 34.

Creditor is defined as “a person who has a claim”; Debtor is defined as “a person who is liable on a claim.” A claim, more instructively, is defined as “a right to payment, whether or not the right is reduced to judgment, liquidated, unliquidated, fixed, contingent, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.” N.J.S.A. 25:2-21.

“Asset [is] property of a debtor [i.e., person liable on a claim], but … does not include a. property to the extent it is encumbered by a valid lien; b. property to the extent it is generally exempt under no bankruptcy law; or c. an interest in property held in tenancy by the entireties to the extent it is not subject to process by a creditor holding a claim against only one tenant.” N.J.S.A. § 25:2-21

N.J.S.A. 25:2-26 lists the factors used to determine actual fraudulent intent:

(1) The transfer or obligation was to an insider;
(2) The debtor retained possession or control of the property transferred after the transfer;
(3) The transfer or obligation was disclosed or concealed;
(4) Before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit;
(5) The transfer was of substantially all the debtor's assets;
(6) The debtor absconded;
(7) The debtor removed or concealed assets;
(8) The value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred;
(9) The debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred;
(10) The transfer occurred shortly before or shortly after a substantial debt was incurred; and
(11) The debtor transferred the essential assets of the business to a lienor who transferred the assets to an insider of the debtor.

All these factors need not be present to prove fraud. In fact, the Court found that in certain cases, the presence of a one factor may be sufficient. *Gilchinsky v. National Westminster Bank N.J.*, 159 N.J. 463 (1999).

iii. Attorney Liability

An attorney's liability to third parties "comports with general principles of tort law." *Petrillo v. Bachenberg*, 139 N.J. 472, 484 (1995) Cases finding attorney liability are fact specific. *But see Barsotti v. Merced*, 346 N.J. Super. 504, 518 (App. Div. 2002), for a finding that the attorney was not liable where the attorney did not “actively conceal or alienate” the assets from the creditor and, further, the attorney had no obligation to report to the creditor that the debtor came into possession of additional assets.

Civil conspiracy to commit fraud is a cause of action. In *Banco Popular North America v. Gandi*, 184 N.J. 161 (2005), an attorney assisted the client in transferring assets to the client’s spouse while guaranteeing loans from business with those assets. Business failed; client was insolvent. Where there was a fraudulent transfer and the defendant knew the transfer was fraudulent and the defendant agreed to assist in the transfer, the defendants will be jointly liable as a co-conspirator.

The Third Circuit held that an attorney may be sued for aiding a fraudulent transfer in New Jersey in *Morganroth v. Norris, McLaughlin*, 331 F.3d 406 (3d. Cir. 2003).

4. **Life Estate Purchases**

Under the DRA, the purchase of a residence property life estate is to be included in the definition of "assets" unless the purchaser resides in the home for at least one year after the date of purchase. 42 U.S.C. § 1396p(c)(1)(J). In addition to DRA requirements, New Jersey Medicaid has begun to “informally” take the position that in the case of a parent who purchased a life estate in a child’s residence, the child must pay rent to the parent.
B. **Matrimonial Settlements and Public Benefits**

1. **W.T. v. Div. of Med. Assistance & Health Servs. and Ocean County Bd. of Social Servs., 391 N.J. Super. 25 (App. Div. 2007)** addressed the denial of Medicaid eligibility where equitable distribution under a property settlement agreement resulted in more than half of the property distributed to the non-applicant spouse. The Appellate Division reversed the final decision by the Division of Medical Assistance and Health Services (“DMAHS”) denying Medicaid benefits to a 59-year-old nursing home resident who was paralyzed following a medical treatment, because the property settlement agreement between him and his non-applicant wife provided more than 50% of the marital assets to his wife. Disregarding accepted principles of matrimonial law, Medicaid deemed the property settlement agreement a transfer of assets and imposed a penalty period of ineligibility. The Appellate Division held that a property settlement agreement providing for a distribution of marital assets favoring the non-applicant spouse did not trigger a transfer of assets because the division of assets was rationally related to equitable distribution principles independent of Medicaid eligibility requirements. The Court held that all DMAHS rules established by “in-house” policy violate the Administrative Procedure Act. Further, the Court found invalid as contrary to New Jersey’s matrimonial law DMAHS’ policy that equitable distribution of less than 50% of marital assets to an applicant spouse within the Medicaid look-back period (the 36 or 60-month period prior to an applicant’s eligibility during which asset transfers of less than fair market value will result in a Medicaid ineligibility period) is a *per se* transfer of assets triggering a Medicaid ineligibility period.

The W.T. Court relied on a 1995 New Jersey Supreme Court decision holding that Medicaid must recognize a state court order effecting equitable distribution. **L.M. v. State of New Jersey, Div. of Med. Assistance & Health Servs., et al., 140 N.J. 480 (1995)**. In L.M., the Medicaid applicant’s pension was distributed to the non-applicant spouse pursuant to a qualified domestic relations order that named the non-applicant spouse the alternate payee of the nursing home spouse’s pension benefits. Medicaid, however, denied benefits, deeming the pension available income to the Medicaid applicant despite the order. The Court held that the qualified domestic relations order shifted *ownership* of the pension to the non-applicant spouse under equitable distribution and thus was not available income to the Medicaid applicant spouse.

J.P., a 48-year old disabled nursing home resident who received Medicaid benefits, was sued for divorce. At her request, the Family Part judge created a special needs trust for her benefit. The subsequent divorce judgment incorporated a Spousal Agreement that required J.P.’s husband to pay the equitable distribution and monthly alimony to the trust. The county Board of Social Services then notified J.P. that the alimony was considered income which must be paid to the nursing home. J.P. appealed the determination and, following a hearing, an administrative law judge held that the alimony was received by the trust and was, therefore, not income to J.P. who had no legal right to receive it. DMAHS reversed the ALJ decision and J.P. appealed the final agency decision.

The Appellate Division reversed the final agency decision and immediately reinstated J.P.’s Medicaid benefits. The Court held that J.P.’s “special needs trust was a legitimate Medicaid planning vehicle for which the Federal and state Medicaid laws clearly provide” and alimony paid to the trust pursuant to a court order is not considered income for Medicaid purposes and a Medicaid recipient’s benefits cannot be reduced by the amount of alimony paid to the special needs trust.


A community spouse, who was allocated a portion of her institutionalized spouse’s income to increase her monthly income to the minimum monthly maintenance needs allowance (MMMNA) as provided under the Medicare Catastrophic Coverage Act of 1988 (U.S.C.A. § 1396r-5(d)) and New Jersey regulations (N.J.A.C. 10:49-1.1 et seq.), instituted an action in the Family Part for separate maintenance in an amount equal to the institutionalized spouse’s remaining net income. On June 13, 2007, the Appellate Division held that the Family Court action was invalid as parallel litigation and a form of forum shopping. The court also held that the standards for awarding spousal support under N.J.S.A. § 2A:34-24 would apply after the institutionalized spouse was eligible for Medicaid, even if it resulted in a higher award than that permitted by New Jersey Medicaid regulations.

C. NEW JERSEY ESTATE TAX CHANGES

1. NEW REGULATIONS- The New Jersey Division of Taxation adopted new regulations to the Transfer Inheritance and Estate Tax Act on January 7, 2008. The regulations, which were proposed on October 1, 2007 (See 39 N.J.R. 4106(a)) and adopted without change, revise sections of the Simplified Tax System and Out of State Property regulations.
(a) **Simplified Tax System**—Estates that are not required to file federal Form 706, may choose one of two methods to file the New Jersey IT-Estate return: (i) the Form 706 method or (ii) the simplified form method. The simplified method must produce a tax liability similar to the Form 706 method. N.J.S.A. 54:38-1.a(2)(a)(ii). To further that requirement, the regulation was revised for purposes of determining the gross estate under the simplified method to add the following new “catch all” phrase and include:

“Any other property includable in the Federal gross estate under the provisions of the Internal Revenue Code in effect on December 31, 2001;” N.J.A.C. 18:26-3A.3(a)6.

(b) **Out-of-State Property**—The regulations provide the following new methodology for calculating the reduction of the New Jersey estate tax attributable to out-of-state tangible and real property.

“(a) The tax, as computed in N.J.A.C. 18:26-3A.2, shall be reduced by:

1. The portion of said tax that is attributable to property located outside New Jersey. The amount of the tax reduction is calculated by multiplying the tax due on the entire gross estate wherever located by a fraction, the numerator of which is the gross value of property located outside the state and the denominator of which is the New Jersey entire gross estate, wherever located. In general, for purposes of the calculation described in this paragraph, intangible personal property is considered to be located in New Jersey; and

2. The inheritance, succession or legacy taxes actually paid this State in respect to any property owned by such decedent or subject to such taxes as part of or in connection with the estate.”

N.J.A.C. 18:26-3A.4

Although the stated purpose of the change is to clarify that certain property not located in New Jersey is not subject to the New Jersey estate tax, comments to the proposed regulations noted that the new rule does not give a clear definition of out-of-state property. The comments expressed concern with the treatment of a decedent’s interest in an LLC or revocable trust that owns out-of-state real property. The regulation does not discuss whether such interests would be treated as intangible property and, therefore subject to New Jersey tax. See 39 N.J.R. 4106(a) and 40 N.J.R. 193(b).
2. **New Jersey “QTIP”** - The New Jersey Division of Taxation proposed new regulations to the Transfer Inheritance and Estate Tax Act on December 17, 2007 purportedly to bring the transfer inheritance and estate tax rules into compliance with the Supreme Court decision in *Lewis v. Harris*, 188 N.J. 415 (2006) and the 2007 Civil Union Act found at N.J.S.A. 37:1 et seq. 39 N.J.R. 5185(a). The regulations, which have been adopted and are effective for decedents dying after April 5, 2008, amend N.J.A.C. 18:26-3A.8 in part, as follows:

“(d) In those cases where a taxpayer makes an election for Federal estate tax purposes, a like election must be made for New Jersey estate tax purposes. Assets and deductions must be treated in the same manner for both Federal and New Jersey estate tax purposes[.] with the following exceptions:

1. In those situations where the decedent is survived by a spouse and a Federal estate tax return is required to be filed, a Qualified Terminable Interest Property (QTIP) election which does not reduce the Federal estate tax liability is not given effect for New Jersey estate tax purposes. In those situations where a Federal estate tax return is not required to be filed, a QTIP election is not permitted for New Jersey estate tax purposes as the property effectively passes as part of the Federal taxable estate.

2. In those situations where a decedent is survived by a civil union partner on or after February 19, 2007, and a Federal estate tax return is required to be filed, a New Jersey QTIP election may be made provided that the election would have reduced the Federal estate tax liability had the decedent been survived by a spouse and the election been made for Federal purposes. In those situations where a Federal estate tax return is not required to be filed, a QTIP election is not permitted for New Jersey estate tax purposes as the election would not have been permitted had the decedent been survived by a spouse.”

3. **Estate of Stevenson v. Dir., Div. of Taxation, Docket No. 008300-2007 (Tax Court February 26, 2008).**

Decedent’s gross estate totaled $1,752,258. Her Will provided for the division of her estate into the marital and non-marital shares. The non-marital share, which passed to her children and grandchildren, was to equal the maximum amount that could pass free of state and federal estate tax. The balance was to pass to her husband as the marital share. The Will also directed that all taxes, on both probate and nonprobate assets, were to be paid from the residuary estate. The non-marital share was not
funded because a nonprobate asset with a value in excess of $675,000 passed to decedent’s children. In calculating the marital share, the state deducted from the residuary estate the amount of federal estate tax that would have been due if the decedent died in 2001, prior to the New Jersey estate tax decoupling from the federal estate tax, reducing the marital share (and accompanying marital deduction amount) by more than $345,000 and increasing the New Jersey estate tax by almost $25,000. Despite the estate’s contentions that the “hypothetical” and “imaginary” federal estate tax should not be included in the calculation, summary judgment was granted to the Director. The Tax Court held that, in calculating the amount of New Jersey estate tax due, New Jersey statute requires deducting from the residuary estate (as provided under the tax clause of the Will) the amount of federal estate tax which would have been due had the decedent died prior to December 31, 2001, despite the fact that no federal estate tax was actually due on this estate because of tax law changes. See the Economic Growth and Tax Relief Reconciliation Act of 2001, P.L. No. 107-16 §§ 511-532, 115 Stat. 38, 70-75 (2001). The deduction of the “hypothetical” federal estate tax from the residuary estate in the calculation of the New Jersey estate tax reduced the amount of the residuary estate eligible to pass to the decedent’s husband eligible for marital deduction and free of estate tax. That reduction resulted in additional New Jersey estate tax, which in turn further reduced the residuary estate eligible for the marital deduction. At the same time, the Tax Court rejected the estate’s argument that, in computing the New Jersey estate tax, only the actual amount of federal estate tax paid by the estate should have been deducted from the residuary estate.


New Jersey’s Supreme Court decided that the doctrine of manifest injustice bars the retroactive application of New Jersey’s July 2002 estate tax decoupling statute, found at N.J.S.A. §54:38-1, to estates of decedents who made their Wills in 1998 and 1999 based on the laws in effect at the time and who died after December 31, 2001.

D. Additional Updates

1. Revised Uniform Anatomical Gift Act (S-3047) was voted out of committee on February 14, 2008. The bill, introduced by Senator Richard J. Codey on January 3, 2008 with the intention of significantly increasing organ donations, would make New Jersey the first state to require an applicant for a driver’s license or state identification card to make an organ donation decision as part of the application. If the applicant decides to become an organ donor, the information is placed conspicuously on the driver’s license or
identification card and added to the organ registry. If the applicant is not ready to make that decision (or does not want to make that decision public), then he or she is asked to designate a surrogate decision maker to decide at a future time. If the applicant does not choose a surrogate decision maker, he or she must acknowledge the importance of making an organ donation decision by checking off a box on the application. The applicant then receives a personal identification number that must be presented to the Motor Vehicle Commission before he or she can receive a new or renewed driver’s license or identification card.


A.H. applied for nursing home Medicaid benefits for his father who, on reapplication following an initial denial, was found to be eligible retroactive to the original application date (March 2002). A few months later, A.H. obtained an $85,200 mortgage loan on his parents’ condominium with a power of attorney, which he deposited in his parents’ bank accounts. A.H. then wrote himself a $35,000 check from those funds. When A.H. applied for Medicaid benefits for his mother the following day, he did not disclose her ownership in the bank accounts. A.H. wrote additional checks to himself from the bank accounts and claimed the $35,000 check was in repayment of a loan he made to his parents in November 1988. The Appellate Division affirmed a final agency decision imposing a penalty period of Medicaid ineligibility finding the proofs of the loan, A.H.’s testimony and a signed note that was not notarized and unrecorded, were not credible. The Court also found A.H. personally liable for the Medicaid benefits paid on behalf of his parents during the appeal process because he did not take steps to liquidate his parents’ condominium, elected to continue Medicaid benefits during the appeal and personally benefited from his parents’ assets while Medicaid benefits were incorrectly paid on behalf of his parents.


An application for DDD residential services by a 55-year old developmentally disabled person previously cared for by his parents was rejected because he did not meet the regulatory requirement that he suffered substantial functional limitation in three major life areas before age 22. The Supreme Court held that there is no statutory requirement that the applicant develop substantial functional limitations before the age of 22 and the Division of Developmental Disabilities’ (“DDD”) regulatory
requirement exceeded its authority and was invalid. Further, the Court found that DDD’s, rejection of evidence of disability offered by the applicant’s family as “anecdotal” and not documentary was arbitrary and inappropriate.

4. **SOCIAL SECURITY ADMINISTRATION DECISION-PS 01825.039**

The principal of a special needs trust established by the mother of a 23-year old Supplemental Security Income (SSI) beneficiary with the proceeds of his personal injury settlement was counted as a resource. The trust provided that the trustee had discretion over distributions and, on the beneficiary’s death, Medicaid would be reimbursed. Social Security determined that the trust did not meet the requirement under 42 U.S.C. §1396p(d)(4)(A) that the trust be established by a parent, grandparent, legal guardian or court because the beneficiary was a competent adult and Social Security requires that the person establishing the trust must have legal authority over the trust funding assets otherwise he or she is merely the agent of the disabled beneficiary. As a result of the resource determination, Social Security found that monthly annuity payments made to the trust as part of the personal injury settlement are considered unearned income as they are made.

This determination was made by the Social Security Administration’s Regional Chief Counsel in Ohio. New Jersey’s regional Social Security office has not yet made a comparable determination.

5. **BOWMASTER V. CLAIR, 933 A.2d 86 (PA. SUPER. CT. 2007)**

A special needs trust for the benefit of a disabled beneficiary was not required to reimburse Medicaid for benefits paid during the minority of the beneficiary. The Court held that the true beneficiary of those benefits were her parents who had an obligation to support their daughter. Medicaid reimbursement is to be made only for those benefits paid after the beneficiary reached majority.

6. **IN THE MATTER OF QUARG, 397 N.J. SUPER. 559 (APP. DIV. 2008)**

Decedent and his wife lived together for three years and thereafter were estranged for more than 40 years. The couple never divorced and the only legal proceedings in the matter were for visitation and child support. At the same time, decedent had a 43 year relationship with his companion during which time they had a son, purchased a home together (as husband and wife on the deed), listed themselves as husband and wife on health insurance applications and lived together continuously until decedent was
hospitalized for his final illness. Decedent’s companion sought a share of decedent’s estate claiming that she would be unjustly impoverished if decedent’s estranged wife were permitted to inherit from the estate. The Appellate Division reversed the trial court and held that a constructive trust over the companion’s intestate share of decedent’s estate was not warranted, and remanded the matter for a determination on whether decedent made an implied promise to adequately provide for his companion for her lifetime under contract law.

7. **UPDATE OF ELDER AND DISABILITY NUMBERS**

(a) Medicaid

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<td>Monthly Income Cap</td>
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<td>Community Spouse Resource Allowance (CSRA)</td>
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(b) Medicare

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<td>Part B Premium</td>
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### Monthly Premium and Yearly Income

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<th>Monthly Premium</th>
<th>Single</th>
<th>Married Couple (Filing Jointly)</th>
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<td>$96.40</td>
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<td>$122.20</td>
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<td>$199.70</td>
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<td>$238.40</td>
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<th>Monthly Premium</th>
<th>Yearly Income, Married Couple Filing Separately</th>
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<tr>
<td>$96.40</td>
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<td>$199.70</td>
<td>$82,001-$130,000</td>
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<tr>
<td>$238.40</td>
<td>Above $130,000</td>
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*(c) Long-Term Care Insurance*

Daily Benefit Amount Excluded from Income Taxation

I.R.C. §7702B(a)(2) $270

Premium Amounts Qualified for Income Tax Medical Expense Deduction I.R.C. §§ 213 and 7702B.

- 40 or less $310
- More than 40 but under 51 $580
- More than 50 but under 61 $1,150
- More than 60 but under 71 $3,080
- Over 70 $3,850