Estate Planning in the Age of Stepfamilies

More than 4 in 10 Americans have at least one step-relative in their family – either a stepparent, a step or half sibling or a stepchild – according to the Pew Research Center. The National Center for Family and Marriage Research estimates that about one-third of all weddings in America create stepfamilies.

A recent trust case from North Dakota highlights the importance of taking current and potential step-relationships into account when planning your estate. William and Patricia Clairmont created two trusts for their grandson, Matthew. In both trusts, "the brother and sisters" of Matthew were contingent beneficiaries (meaning they would be the trust beneficiaries if Matthew died).

After the trusts were created, the Clairmonts' daughter, Cindy (Matthew's mother), divorced Matthew's father, Greg, and Greg remarried and had two children with a second wife. In March 2011, Matthew died suddenly and unexpectedly at the age of 25 without a wife, children or a will.

Under North Dakota law, Greg's two children with his second wife were technically "brothers and sisters" of Matthew and, thus, eligible beneficiaries under the trusts. The Clairmonts argued for an interpretation of the trust that would exclude Matthew's stepsiblings as beneficiaries or, alternatively, for reformation of the trust to include language that only lineal descendants of the Clairmonts could benefit from the trusts.

Ultimately, the North Dakota Supreme Court granted the Clairmonts' petition to reform the trusts based on evidence that the Clairmonts made a mistake of law by interpreting the phrase "brothers and sisters" to include only full blood

siblings and based on testimony by the Clairmonts themselves on their intention to benefit their lineal descendants alone.

Although things turned out well for the Clairmonts in the end, it took much time and money to get there. The case stresses the importance of addressing step-relations in your estate plan whether or not you are already a member of a stepfamily.

To read the May 28, 2013 decision, *In re Matthew Larson Trust Agreement*, click here.

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Have You Planned for State Estate and Inheritance Taxes?

Although most people's estates aren't large enough to be affected by the federal estate tax, residents in many state have to consider how state taxes may reduce their estates. Several states have their own estate tax, which can affect much smaller estates than the federal estate tax does. In addition, some states impose an inheritance tax on beneficiaries of an estate.

The federal estate tax exemption is currently $5.25 million for an individual, so most estates are exempt. However, 15 states (Connecticut, Delaware, Hawaii, Illinois, Maine, Maryland, Massachusetts, Minnesota, New Jersey, New York,

Oregon, Rhode Island, Tennessee, Vermont, and Washington) and the District of Columbia currently have separate state estate taxes, and six states have an inheritance tax (Iowa, Kentucky, Maryland, Nebraska, New Jersey, and Pennsylvania). The numbers change constantly. In recent years, the trend has been for states to eliminate such taxes. For example, Tennessee is currently phasing out its estate tax, which is set to end in 2016.

If you live in one of the states with an estate tax, you need to take the tax into account when planning your estate. While some states (e.g., Delaware and Hawaii) exempt the same amount as federal law, other states' estate taxes can affect much smaller estates. For example, New Jersey taxes estates worth more than $675,000 and Oregon taxes estates of more than $1 million. Most states with an estate tax exempt the first $1 million to $2 million of an estate's value. To find out whether your state has an estate tax and how much it is, click here.

Another state tax to take into account when planning your estate is the inheritance tax. An inheritance tax is a tax on the person receiving an inheritance. Spouses are usually exempt from the tax, and in some states, children are as well. Charitable beneficiaries may also be exempt. Usually, the less closely related the beneficiary, the higher the tax. Even if the beneficiary doesn't live in a state with an inheritance tax, if the person who died resided in an inheritance tax state, the beneficiary can still be taxed. For more information about inheritance taxes, click here.

You have several options for avoiding state estate and inheritance taxes, including creating a trust or gifting money. Talk to your attorney to find out the best solution for you. Because the law is constantly changing, even if you have an estate plan, you should check with your attorney to ensure your plan does not need updating.

Should You Prepare a Medicaid Application Yourself?

Whether you should prepare and file a Medicaid application by yourself or should hire help depends on answers to the following questions:

- How old is the applicant?
- How complicated is the applicant's financial situation?
- Is the individual applying for community or nursing home benefits?
- How much time do you have available?
- How organized are you?

Medicaid is the health care program for individuals who do not have another form of insurance or whose insurance does not cover what they need, such as long-term care. Many people rely on Medicaid for assistance in paying for care at home or in nursing homes.

For people under age 65 and not in need of long-term care, eligibility is based largely on income and the application process is not very complicated. Most people can apply on their own without assistance.

Matters get a bit more complicated for applicants age 65 and above and especially for those of any age who need nursing home or other long-term care coverage. In these cases, availing yourself of the services of an attorney is practically essential.

Medicaid applicants over age 65 are limited to $2,000 in

countable assets (in most states). It's possible to transfer assets over this amount in order to become eligible, but seniors need to be careful in doing so because they may need the funds in the future and if they move to a nursing home, the transfer could make them ineligible for benefits for five years. Professional advice is also crucial because there is a confusing array of different Medicaid programs that may be of assistance in providing home care, each with its own rules.

All of that said, the application process itself is not so complicated for community benefits (care that takes place outside of an institutional setting, such as in the beneficiary's home). In short, those over 65 in many cases will need to consult with an elder law attorney for planning purposes, but they or their families may be able to prepare and submit the Medicaid application themselves.

But submitting an application for nursing home benefits without an attorney's help is not a good idea. This is because Medicaid officials subject such applications to enhanced scrutiny, requiring up to five years of financial records and documentation of every fact. Any unexplained expense may be treated as a disqualifying transfer of assets, and many planning steps – such as trusts, transfers to family members, and family care agreements – are viewed as suspect unless properly explained. Finally, the process generally takes several months as Medicaid keeps asking questions and demanding further documentation for the answers provided.

Many elder law attorneys offer assistance with Medicaid applications as part of their services. This has several advantages, including expert advice on how best to qualify for benefits as early as possible, experience in dealing with the more difficult eligibility questions that often arise, and a high level of service through a long, grueling process. The one drawback of using an attorney rather than a lay service is that the fee is typically substantially higher. However, given the high cost of nursing homes, if the law firm's assistance

can accelerate eligibility by even one month that will generally cover the fee. In addition, the payments to the attorney are generally with funds that would otherwise be paid to the nursing home – in other words, the funds will have to be spent in any event, whether for nursing home or for legal fees.

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The U.S. Supreme Court Rules Gay Spouse Is Entitled to Estate Tax Refund

The U.S. Supreme Court has ruled that a key provision of the Defense of Marriage Act (DOMA) is unconstitutional, clearing the way for the surviving spouse of a lesbian couple to receive a refund of the taxes she was forced to pay because the federal government did not consider her married to her spouse.

Although the ruling does not create a national constitutional right to same-sex marriage, it does allow same-sex couples in states that legally recognize their marriages to receive a host of federal benefits that were previously denied them, such as being able to inherit from a spouse without paying federal estate tax.

Edith Windsor and Thea Spyer became engaged in 1967 and were

married in Canada in 2007, although they lived in New York City. When Ms. Spyer died in 2009, Ms. Windsor had to pay Ms Spyer's estate tax bill because of DOMA, a 1996 law that denies federal recognition of gay marriages. Although New York State considered the couple married, the federal government did not and taxed Ms. Spyer's estate as though the two were not married. Ms. Windsor sued the U.S. government seeking to have DOMA declared unconstitutional and asking for a refund of the more than $363,000 federal estate tax she was forced to pay. As previously reported, a federal court judge from the U.S. District Court for the Southern District of New York ruled that there was no rational basis for DOMA's prohibition on recognizing same-sex marriages.

In a 5-4 decision, the U.S. Supreme Court declared that DOMA is an unconstitutional deprivation of equal liberty under the Equal Protection Clause of the Fifth Amendment. Noting that states have the power to define and regulate marriage, the Court held that DOMA discriminates against same-sex couples who are legally married in their state. According to the court, "DOMA instructs all federal officials, and indeed all persons with whom same-sex couples interact, including their own children, that their marriage is less worthy than the marriages of others. The federal statute is invalid, for no legitimate purpose overcomes the purpose and effect to disparage and to injure those whom the State, by its marriage laws, sought to protect in personhood and dignity."

The ruling will have many implications for same-sex couples with regard to federal estate taxes, gift taxes, Social Security benefits, and IRA beneficiary rollover rules, and more than 1,000 other federal benefits. The decision means that same-sex couples who are legally married must now be treated the same under federal law as married opposite-sex couples, at least in states that recognize same-sex marriage.

Complicating matters is that the case brought to the Supreme Court did not challenge another provision of DOMA that says no

state must recognize a same-sex marriage from another state. If a couple married in a state that recognizes same-sex marriage moves to a state that does not, not all federal rights and benefits accorded married couples will apply because some benefits – like Social Security, for example – are contingent on whether the marriage is considered valid in the state where the couple currently lives.

For this to change, Congress will have to pass new laws and/or President Obama will have to change regulations. But in the meantime, Edith Windsor can expect a check from the U.S. Treasury for $363,053 – plus interest.

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Medicaid Annuities

Annuities Bought for Medicaid Applicant's Spouse Are Neither Income Nor Resource

A U.S. district court has held that the annuities a Medicaid applicant purchased for his wife cannot be considered as either assets or income when determining Medicaid eligibility. *Jackson v. Selig* (U.S. Dist. Ct., E.D. Ark., No. 3:10–CV–00276–BRW, March 13, 2013).

Richard Jackson lived in a nursing home and applied for Medicaid benefits. The state denied Mr. Jackson's application because he had more than $300,000 in available resources. Mr. Jackson purchased an annuity for his wife for $248,949.09 and a smaller annuity for himself, and then reapplied for

benefits. The state found Mr. Jackson transferred resources for less than fair market value and issued a 69-month penalty period

Mr. Jackson sued the state in federal court. The state filed a motion to dismiss, but the district court denied the motion. Both parties asked for summary judgment. (Mr. Jackson died during the pendency of the lawsuit.)

The U.S. District Court for the Eastern District of Arkansas grants summary judgment to Mr. Jackson. The court holds that because the annuities complied with federal Medicaid law, they cannot be considered as assets when determining Medicaid eligibility. In addition, the court rules that the annuity payments were made to Mr. Jackson's wife, so the annuity payments are not income or resources available to Mr. Jackson.

For the full text of this decision, click here.

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