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Legislative Testimony
House Judiciary Committee
HB 2166

Mr. Chairman; Members of the Committee:

My name is Ron Smith. I am a partner with Smith, Burnett, Larson & Butler, LLC, of Larned, Kansas. Our four-person firm is well-established in Central Kansas. Glee Smith, Jr. began practicing law in Larned in 1947 along with Maurice Wildgen, a former President of the Kansas Bar Association and who practiced in Larned since 1933 during the early days of the Depression. Don Burnett has practiced in Larned since 1958, and Jerry Larson since 1973. I have been in Larned since 2005 and Jacque Butler, our newest partner, since 2009. We have handled many probate and trust cases over time.

Part of my probate practice is working with the Kansas Department of Health & Environment-Division of Health Care Finance and Medicaid recovery cases. I work with the Kansas Estate Recovery Program in most counties in Western Kansas. I believe the recovery program, when it is understood, is fair. When people who do not have the means in their advanced age to provide long term medical care for themselves, the taxpayers – through Medicaid -- step in. As you know, it is the last years and months of life that are the most expensive, medically. In return, the federal government requires states having Medicaid programs to recoup costs from the remaining assets of the recipient.

The basis of the entire program of recovery is found at page 10, lines 6-10 of the bill.

> (3) By applying for or receiving medical assistance under the provisions of article 7 of chapter 39 of the Kansas Statutes Annotated, such individual or such individual's agent, fiduciary, guardian, conservator, representative payee or other person acting on behalf of the individual consents to the following definitions of estate and the results therefrom:

There often are remaining assets. However, sometimes after an heir helps mom or dad obtain Medicaid assistance, those same heirs want to keep the real estate but not lose the Medicaid support from the state. The program is a choice. Either the heirs utilize Medicaid and give up the property (to the extent of Medicaid assistance to their loved ones) or the heirs pay out of pocket for Mom or Dad's long term care, in which case they can have an ordinary probate that keeps the property among the heirs.

It is not unethical to provide the heirs with transfer avoidance devices – usually transfer on death deeds or trusts. Or, on occasion, selling the property to their children for a long term low-interest rate purchase contract. The statutes provide if there is fair market value involved in these purchases, it is presumed the proceeds go to the seller to offset later medical needs.

Unless real estate is subject to a valid mortgage (again FMV involved) and the mortgage covers most of the equity in the house, however, the state's recovery interests remain. In my practice, about 80% of the time there is a small house available to sell or auction off.

The proceeds that are recovered rarely cover the total value of Medicaid funds provided, but even if the state recovers part of the Medicaid expenditures, it is a program whose recovery efforts are worthwhile. The funds recovered by the Estate Recovery Program, to the tune of several million dollars a year go back into the Medicaid program, and are therefore an important funding source for Kansas Medicaid. Strengthening the recovery aspect of this program is important. That's what HB 2166 does.

There are two key definitions in this bill that are current law and must be preserved. The first is at page nine, lines 30-32. It is part of K.S.A. 39-709(g)(2):

> **"Transfers of real or personal property by recipients of medical assistance without adequate consideration are voidable and may be set aside."**

What this means is that if a recipient or someone acting with power of attorney for the recipient deeds the property to a third party for less than adequate consideration, the state can "claw back" property that is set over to the heirs or third parties unless there has been adequate consideration paid. Sometimes our recovery probate actions utilize this provision to pull the property back into the estate for further probate orders on that property. Typically, we then get court permission to auction the property – or sell it outright for Fair Market Value to the heirs.

The second definition is at page 10, lines 16-27. This is K.S.A. 39-709(g)(3)(B). This portion defines what probate avoidance devices can be pulled back into the medical assistance estate, the value of which is made available for estate recovery by the state. The medical assistance estate includes some title transfer devices that ordinarily are not part of probate – things like trusts, life estates, joint tenancy property, transfer on death deeds and Payable on Death accounts. It is these probate avoidance devices which we pull back into the estate, and get court orders on reducing this property to cash, then reimburse the state as much of the claim as possible.

These two definitions should remain intact if you want to keep the overall recovery program strong.

Let me highlight my testimony. The reform items included in this bill are:

1. The time to file an estate <u>as a creditor</u> is expanded from 6 months to one year. These changes begin on page 16 of the bill.

2. The state is allowed to use the Small Estates Affidavit, 59-1507b.

3. The mandatory notice of filing a probate-style action is expanded to include notification to the state by a trust, and,

4. The adoption of a method for calculating the value of life estates

I.

One reform in the bill **expands the time for all creditors to file a probate after decedent's death to one year**. Current law is six months. "Creditors" includes the state.

By the time I get the information from Topeka, the six months has nearly run. Either the state needs help getting the information in time to make a decision within the current six months, or it needs more time than the current six months to research the decedent's estate to see if there is anything there. This expansion helps the state, but also other creditors.

The six month filing period is for filing a will, and it is used as an estate planning tool to nullify a will that might be "out there," and also cut off creditors, who must file a creditor probate within six months or lose their claim. The estate recovery program is a creditor and it is at a disadvantage because it is often several months after death before the state agencies can determine who died, the amount of the state's claim, what property there might be available for recovery, and whether that property is encumbered with mortgages or whether fair market value was given. Much of the information comes from heirs, who are reluctant to assist the state. If Mr. Sherber's office has to make last minute decisions without enough information before filing, sometimes we end up filing an action with missing or incomplete information.

If the heir can string it out six months, then there is no recovery action and they can divide up the assets. A year would allow enough time to research and file these actions, the timeframe is not an overly burdensome, and it strikes the right balance between the interests of the heirs and the interests of creditors such as the state.

II.

Under this bill the state is allowed to use the **Small Estate affidavit process, KSA 59-1507b, found** at page 18, line 22.

Sometimes all that remains after the death of a recipient of Medicaid is some cash in a bank account, or some capital credits at the local coop. In these types of cases, if the amount of funds is less than a few thousand dollars, a probate estate is not cost-effective for the state to pursue, but yet these otherwise collectable funds cannot be recovered any other way except by probate. Currently the heirs can file these affidavits, thus avoiding probate. Giving the Estate Recovery Program authority to use the small estates affidavit to pursue these assets will solve the problem.

Heirs often utilize the K.S.A. 59-1507b affidavit to obtain this cash. They often submit it soon after their loved one's death. The affidavit form states that the persons who obtain the cash through the affidavit will be responsible for debts of the decedent, but when the heirs live in other states nobody is looking over their shoulder to insure that creditors are paid. The state cannot afford to file a collection lawsuit in another state to recover that small amount of money. The alternative for the estate recovery unit is filing a probate action to get a court order to get the bank to turn over the account the bank is holding to the estate recovery unit. But that is a slow process, like weeding a garden with a bulldozer.

Another problem is that soon after a decedent dies, the estate recovery unit doesn't know which banks might have idle funds. Allowing the state to submit an affidavit is good but unless we know which banks might have the funds, the ERU is left with a shotgun filing of affidavits to all banks in the area. If you get competing affidavits – one from the heirs and one from ERU, the bankers are likely to honor the first affidavit presented to them.

Thus you may want to add to this affidavit section a requirement that the banks take into their possession all affidavits presented to them, but the bank cannot choose which affidavit it honors under 1507b affidavit for 60 or 90 days -- assuming that such a limitation would not offend rules and regulations of the Comptroller of the Currency or the state examiners. Further, using the negotiation authority in K.S.A. 39-709, it might be advantageous to the state to release its affidavit on a bank account in return for assistance by the heirs on a more valuable property, such as an interest in a house or a life estate in farm ground.

But you have to give the state time to develop the affidavit and get it out to the banks. Like Mr. Sherber says, sometimes it can be two or more months before they know a Medicaid recipient has died.

The small estates affidavit process allows the state to utilize the 1507b affidavit process in the name of Medicaid estate recovery.

III.

The **mandatory notice to the state by a trust** whose settler has died so the estate recovery office can check for Medicaid use is at **Page 15, Line 14.** Probate Executors and administrators now make these notifications. It is mandatory that the probate administrators file notice in the newspaper of the opening of an estate. But it is permissive under K.S.A. 58a-818 to file the same sort of trust administration action WITHOUT notice in the newspaper. I've never understood that difference between publication involving probate of a will and publication involving the probate of a trust. Most trust administration is done with a notice to creditors in the newspaper.

There is no reason a trustee can't notify the state, even if there is no newspaper publication and even if the deceased person is wealthy and never did use Medicaid. It could be done by private letter. Most of the lawyers winding up a trust also are aware that if probating a will they must give Mr. Sherber's office notice. They can make a routine notification when trustees publish notice to creditors as they are winding up the trust.

Don't let trustees or lawyers representing trustees tell you this isn't necessary. One of the more abused areas of current probate law is trust administration – even trusts where there is a wealthy individual involved and no Medicaid involvement whatever.

This change won't hurt trust administration. The requirements in this bill for notification are fair to trusts has the provision that if there is no response from the state after 30 days, the trust can proceed without fear of a claim being made. **(Page 18, lines 14-21)**

IV.

The life estate definition is at page 12, line 10. Sometimes the decedent's only interest in land is a life estate in property. The value of the life state is based on the value of the property.

I have had five cases where the life estate of an individual was the primary remaining estate asset. In one of them, a woman had had a life estate for ten years and received money and crop shares from her son. There was enough income there that the crop income exceeded costs of administration and we had to file a 1041 estate income tax return. Yet she was on Medicaid.

In several of the other estates, however, attorneys are fighting us as to the value of the life estate "at death" or shortly before death. Judges are being asked to severely limit the value of the life estate, to the state's detriment of ERU. If judges end up making this decision, you may end up with a checkerboard, different decisions in different district courts.

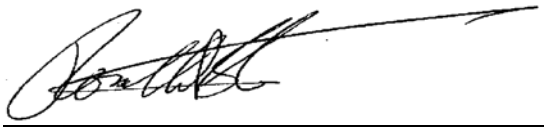
These attorneys argue it is the legislature that should define a life estate, not the judges. We agree that the BETTER format is for policy makers to define this term. Thus we have this provision in the bill. You are delegating to the executive branch rule and reg authority on this topic.

I told you earlier the importance of the sentence at Page 10, line 22. The legislature decided some years ago that life estates were part of the medical assistance estate. The law presumes you do not legislate a nullity. Courts cannot presume that you said "life estate" but intend the recovered amount be zero.

You are asked in this bill at **Page 12, lines 13-19,** to have the Department prepare a rule and regulation calculating the value of a life estate for this recovery statute. Or, in the alternative, you may want to consider adopting a table yourself and putting it into the statute.

Life estate valuations is an area crying out for legislative guidance as it's a source of much litigation and will be determined by the courts unless the legislature acts.

I appreciate being here today and I'll try to answer questions.



Ronald D. Smith