



Planning for Long-Term Care: New Laws and Regulations

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PRE DEFICIT REDUCTION ACT WHERE WE'VE BEEN.....

- Transfers-look back

Disqualification penalty

- Three (3) year look back for most transfers

- Five (5) year transfer for certain trusts

- Penalty imposed as of the first day of the month in which the transfer occurred



Example

Parent transfers \$25,600 to child on January 10, 2005 as a gift. This would render the parent ineligible for 100 days from January 1 assuming a divisor of \$256/day. On the 101st day, if otherwise eligible, this transfer would no longer count against the parent in computing eligibility for assistance, i.e. April 12, 2005.

These rules still apply to transfers which occurred prior to February 8, 2006



.....WHERE WE ARE NOW

A quick review of the changes

- Transfers-look back

***Applies to transfers
made On or After
February 8, 2006***

(transfers prior to
February 8, 2006
under old rules)

- Five (5) years from
the date of application
for **all** transfers
(whether or not in
trust)



.....WHERE WE ARE NOW

A quick review of the changes

- Disqualification penalty

The penalty for any gifts made at any point in the five year look back will be imposed on the ***later*** of these two dates

Penalty imposed as of the first day of the month in which the transfer occurred

or

The date on which the individual would otherwise be eligible for assistance and would be receiving institutional level of care but for the application of the disqualification penalty



Example

Parent transfers \$25,600 to child on January 10, 2007 as a gift. This would render the parent ineligible for 100 days with a divisor of \$256 per day, but the penalty would be computed not from the date of the gift, but from the date otherwise eligible as set forth previously. If the parent entered the nursing home on January 1, 2011 and was otherwise medically and financially eligible on that date, the parent would still have a 100 day penalty that would run in 2011 and would not be eligible for assistance until April 12, 2011.



Pre-DRA 2005.....

■ Annuities

- Not a countable asset. Not a disqualifying transfer if:
- Irrevocable and Non-assignable
- Names applicant or spouse as beneficiary
- Is immediately payable in equal amounts with no deferral or balloon payments
- Actuarially sound
- **No restriction on successor beneficiary**



Pre-DRA 2005.....

- Home Equity

- Principal residence of an applicant is a non-countable asset irrespective of the equity in such residence

Purchase of Life Estates

- Permitted- no post purchase residency requirement



Annuities.....Post DRA 2005

- Not a countable asset if annuitized.

Not a disqualifying transfer if:

- Irrevocable and Non-Assignable
- Names applicant or spouse as beneficiary
- Is immediately payable in equal amounts with no deferral or balloon payments
- Actuarially sound
- **Commonwealth must be named as the Beneficiary to the extent of benefits paid, unless Community Spouse or minor or disabled child is named, in which case Commonwealth must be contingent beneficiary**
- *These rules do not applied to certain qualified plans*



Post DRA 2005

- Home Equity
 - If the individual's equity in the home exceeds \$750,000, the excess equity is considered countable
 - N/A if any of the following individuals resides in the home-
 - Spouse
 - Minor child
 - Disabled child



Post DRA 2005

- Purchase of a Life Estate
- Permitted, provided that the purchaser resides in the home for at least one (1) year after the date of the purchase of the life estate- if resides in home for less than a year the purchase is a disqualifying transfer



Promissory Notes

- Promise to pay.
- The notes must:
- Have repayment terms that are “actuarially sound” according to publications of the Office of the Chief Actuary of the Social Security Administration
- Provide for payments that are in equal amounts during the term of the loan, and
- Must prohibit cancellation of the balance at death
- It is helpful to have the maker of the note sign their assent to the promissory note “contract”



Promissory Notes

- These rules are designed to make sure that money is lent to family members with expectation of repayment. If the loan does not meet these requirements, the balance owed will be treated as a disqualifying transfer
- If the loan meets these tests but is not actually repaid, it is likely that there would be no disqualifying transfer, but the balance of the loan payments due may be considered a countable asset
- These rules apply to all loans, even those made prior to DRA 2005



What To Do When Your Client is Knocking On The Nursing Home Door Post DRA 2005



For all applicants

- Gather Together all Financial Data and Determine if excess assets
- Consider having applicant execute durable power of attorney/health care proxy (if able to)
- Consider the Purchase of Exempt Assets:
 - Pre-paid funeral
 - Burial Account with \$1500
 - Principal Residence
 - Business/Income Producing Property
 - Purchase of a qualifying interest in residential real estate



Planning for a Married Couple

- Evaluate Assets to Determine if Excess Assets
 - Currently Applicant may have \$2000 and the Community Spouse may have \$101,640 in *countable* assets
- Transfer Assets to Community Spouse
- Purchase Exempt Assets
- Consider using an annuity to convert “assets” to “income”



Planning with Annuities

- Annuities, even after DRA 2005 are *not* countable assets and the purchase of an annuity does not constitute a disqualifying transfer if it meets the rules described in Slide 8 “Annuities.....Post DRA 2005”
- This gives us some planning opportunities



Planning with Annuities

- Married Couple

- Purchase an immediate, irrevocable annuity for the Community Spouse with Excess Assets, **but**
Use the shortest payout period you can obtain to avoid the recovery of benefits by the Commonwealth
Then start planning for the Community Spouse and the possibility of long term care



Planning for the Community Spouse

- ***Once you have obtained eligibility for the Institutionalized Spouse, the job is not done!***
- Update Community Spouse's estate plan- (an "I Love You Will" ***must*** be changed)
Prepare a new Will and Trust, funded by or through the Will, which provides for the Institutionalized Spouse with special needs trust provisions
- Update Durable Power of Attorney- if Institutional Spouse was named, name a new Agent and Alternate
- Change Life Insurance/IRA, Annuities and Transfer on Death Accounts beneficiary designations from Institutionalized Spouse



Planning for an Individual

- Evaluate Assets to Determine if Excess Assets
- Purchase Exempt Assets
 - Frequently the single individual is living in an apartment or with a family member
 - **Consider using an annuity to convert “assets” to “income”**



Planning with Annuities

- Unmarried Individuals
 - Use in situations where the individual does not have a long lifespan (e.g. in hospice) but needs nursing home care
 - The Commonwealth will still receive reimbursement as contingent beneficiary of the annuity to extent it pays benefits, but the Medicaid payment rate to the nursing home is significantly less than private pay rates



Supplemental Needs Trusts

- Supplemental Needs Trusts were codified in the Omnibus Budget Reconciliation Act of 1993 (“OBRA 93”) at 42 USC 1396p
- Trusts created for an individual who is under 65 with their own assets is known as a 42 USC 1396p (d) (4) (a) trust a “(d) (4) (a)”
- Trusts created for an individual that is managed by a charity in a pooled arrangement is known as a 42 USC 1396p (d) (4) (c) trust, a “(d) (4) (c)”



Supplemental Needs Trusts

■ Pooled Trusts (d) (4) (c)

- ✓ Any age
- ✓ Investment managed by charitable entity
- ✓ Requires payback for medicaid benefits upon death of beneficiary
- ✓ Usually requires payment to charity of portion of remainder upon death of beneficiary
- ✓ Established by individual, parent, grandparent, legal guardian or court



Special Needs Pooled Trust

- Excess Assets are transferred to a Special Needs Pooled Trust authorized under 42 U.S.C. 1396p(d)(4)(C)
- Transfer of assets into the trust is *not* a disqualifying transfer
- The assets must be pooled for purposes of investment and management
- Each beneficiary has a separate account within the pooled trust
- The person creating the account has an election regarding the distribution of the remaining balance (if any) upon the death of the disabled person. If the remaining balance in an account is retained by the pooled trust after the death of the beneficiary, then Medicaid is not entitled to be paid back. Any amounts not retained by the pooled trust must be used to reimburse Medicaid for the cost of medical assistance provided to the beneficiary during his or her lifetime.



Pooled Trusts

- The Pooled Special Needs Trust (d) (4) (C) allows an SSI or Medicaid recipient of any age to place their own funds in a trust for their needs if it meets the following conditions:
- The trust is established and managed by a nonprofit association
- A separate account is maintained for each beneficiary of the trust, but, for purposes of investment and management of funds, the trust pools these accounts
- Accounts in the trust are established solely for the benefit of the disabled individual by the parent, grandparent, or legal guardian of such an individual, **by such an individual**, or by a court
- To the extent that amounts remaining in the beneficiary's account upon the death of the beneficiary are not retained by the trust, the trust pays to the State from the remaining amounts in the account an amount equal to the total amount of Medicaid assistance paid on behalf of the beneficiary under the State plan under this subchapter and if there is a balance thereafter, as designated when establishing the trust



Use of Pooled Trusts

- Disbursements made by the pooled trust solely for the benefit of the disabled beneficiary to improve their quality of life
 - Can pay for cable, phone, internet, companionship services, personal needs items, travel, vacation, medical and dental services not covered by Medicaid or Medicare, recreational activities (i.e. movies)
 - Can not pay for food or shelter without an offset of some benefits



Pooled Trusts

- Upon the death of the beneficiary, the pooled trust receives a portion of the remaining assets, Medicaid is reimbursed for the cost of care. If there is any remaining balance, the party establishing the pooled trust account can specify the recipient(s), to receive any remaining balance.



Pooled Trust Example

- Emily is 67 and is a resident of a subacute nursing facility which costs in excess of \$18,000 per month and has huntington's disease. Her parents and grandparents are deceased and she is mentally competent. She has \$400,000.00 of countable assets. She can establish a pooled trust and immediately qualify for benefits. The trust can provide her with the funds to purchase the services and goods described earlier.



Factors to consider in selecting a Pooled Trust

- Ease of obtaining and length of time for obtaining distributions from the trust
- Criteria for distributions from the trust
- Fees charged by the Trust in establishing and maintaining the trust
- How funds in trust are invested
- Review master trust agreement and joinder agreement
- Amount retained by charity upon death of beneficiary



Other uses of trusts in planning for long term care

- Since there is no longer a difference in the look-back period for disqualifying transfers to trusts and other disqualifying transfers, trusts have come back into favor if you have a longer horizon to plan



Nursing Home Care Anticipated in Distant Future

- Nursing home care unlikely in next 5 years
- Standard planning tools in place
 - Financial Power of Attorney
 - Health Care Proxy
 - Will or Will and Revocable Trust



Planning Options Under Current Law and Practice

- Outright gifts to trusted family or friend
 - Sometimes followed by transfer by Donee to revocable (or irrevocable trust if more than one child)
- Transfer (usually the Home) to Irrevocable Income Only Trust



Structure of Outright Gift Plan

- Mama transfers \$100,000 to Child (“C”)
- C holds for at least 30 days or long enough to receive statement in C’s name
- C creates Revocable Trust
 - For the benefit of C while living and competent
 - C is Trustee
 - Upon C’s death or incompetency, to Special Needs Trust for benefit of Mama
 - Upon death of Mama, C can, but need not, make gifts to other heirs



Mama's Personal Results

- Assets reduced by \$100,000
- No access to funds except with consent of C
- No control of distribution of assets upon death
- Assets subject to C's creditors (5 D's)
 - Death
 - Divorce
 - Disability
 - Debt
 - Disaster



MassHealth Results Under Current Law

- 5 Year Disqualification
- After 5 years if C is living, trust assets are not reportable on MassHealth Application because Mama is not a
 - Grantor,
 - Beneficiary, or
 - Trustee
- At Mama's death, trust assets distributed to her beneficiaries if C agrees
- No estate recovery



Tax Results

- Income Tax
- Gift Tax (federal only)
- Estate Tax



Income Tax Results

- All income taxed to child whether in trust or not
- Carryover basis
- Capital gain on sale if applicable



Gift Tax Results

- Federal tax only
- Taxable gift from Mama to Child less annual exclusion amount (\$12,000 per donee)
- No tax if Mama's total taxable gifts are less than \$1,000,000
- Taxable gift from Child (less annual exclusion) to other heirs if gifts made at Mama's death



Estate Tax Results

- Trust property included in C's taxable estate at C's death unless gifted earlier
- Taxable gifts brought back into Mama's and C's Federal and Massachusetts estates
- Federal estate tax applicable exemption amount currently \$2,000,000
- Massachusetts filing threshold currently \$1,000,000



More Than One Child

- Can use one child model but make irrevocable with gifts to others at Mama's death, or
- Multiple grantors on trust
 - Irrevocable without consent of all
 - Multiple Trustees or not
 - Grantor trust as to each grantor
 - More complicated but doable



Income Only Trust Agreements ("IOTAs")

- Keeps lifetime benefit of transferred assets for Mama
- Receives all trust income (not capital gain)
- Mama retains control over distribution of assets at death
- Stepped up basis at death (Query: 2010 and thereafter)



Structure of IOTA Plan

- Mama transfers home to Income Only Trust
- Child or other trusted individual as trustee
- Mama retains income and/or life use of trust property
- Children may be given access to principal
- At her death, trust assets distributed to designated heirs via trust instrument or Special Power of Appointment in IOTA
- Irrevocable transaction



Mama's Personal Results

- Retains lifetime right to use home
- If home sold and replaced, retains right to use replacement home or unit in retirement community
- If home not replaced, retains right to income from proceeds
- Controls distribution to heirs via SPOA
- No exposure to creditors – hers or her children's
- No right to trust principal – but children can have access
- Should not be Trustee but can retain the right to remove and replace Trustee



MassHealth Results Under Current Law

- 5 year disqualification
- Trust reportable on MassHealth application
- Trust income (if any) countable
- Trust principal not countable after 5 years
- No estate recovery



Income Tax Results

- Grantor Trust: Grantor treated as owner for income tax purposes because of retained rights to
 - Income, and
 - Control of distribution of trust principal at death via SPOA. IRC Sections 674, 677
- Income and capital gain/loss taxed to grantor
- No capital gain upon sale of home under IRC Section 121
- Stepped up basis at death (? 2010 and thereafter)



Gift Tax Results

- Incomplete gift due to retained SPOA
- No use of annual exclusion
 - Incomplete gift
 - No present interest
- Federal consideration only
- No Massachusetts gift tax



Estate Tax Results

- Included in Mama's Federal and Massachusetts estates
- No estate tax inclusion in estate of previously deceased child
- Stepped up basis to heirs subject to changes in 2010 and thereafter



Married Couples

■ Option A

- Transfer to one, proceed as above
- Include SNT in IOTA for other if he or she survives grantor

■ Option B

- Create mirror image trusts
- Each holding one half interest in home
- SNT provisions in each IOTA

■ Note other planning options for married couples as discussed earlier



Nursing Home Care Imminent

- Pooled Trusts (previously discussed)
- Transfer to caretaker child, sibling with equity interest in home or disabled child (previously discussed)
- Joint purchase of home
- Joint purchase of income producing property
 - Real estate
 - Closely Held Business (?)



Joint Purchase of Home

- Mama, who does not own home, buys one half interest in Child's home
- Home must be Mama's legal address
- Mama must intend to return home and so state on MassHealth application
- Child must be prepared to have Mama return if medically possible
- Title held as joint tenants with rights of survivorship



MassHealth Results

- Mama's interest in Home non countable asset for purposes of MassHealth eligibility
- Passes to Child at Mama's death free of MassHealth estate recovery
- If Child predeceases Mama, entire value of home subject to estate recovery at Mama's death



Caveats

- Interests of Mama and other owners must be equal
 - 50/50: Mama and Child, or
 - 1/3-1/3-1/3: Mama, Child, Child's Spouse or Partner, or
 - 25/25/25/25: Mama, Child A, B, and C
- Purchase price must be applicable % of FMV or Assessed Value
- Existing mortgagee, if any, must consent
- Mortgage cannot be greater than value of other owner's interest
- No personal liability for mortgage in Mama, but she may have to take subject to mortgage



Joint Purchase of Income Producing Property

- Property producing income necessary to support is a non countable asset
- Rental real estate currently allowed
- Title should be held jointly with rights of survivorship in joint owners (usually children)
- Net income paid out pro rata to owners
- Mama's net income is countable,
- Included in patient paid amount to nursing home



Caveats

- Ownership interests must be equal as with purchase of joint interest in home
- Any mortgage must be on Child's interest only
- Mama's interest not subject to mortgage
- If all joint owners predecease, entire value of property subject to estate recovery



Protected Transfer: Parent to Disabled Child

- Documented disability: Permanent and total disability as defined by the Social Security Administration
- Transfer for sole benefit of disabled child
- Cash, stock, real estate
- Outright transfer vs. transfer to Trust
 - If child receives SSI or other needs-based aid, consider transfer to Supplemental Needs Trust



Supplemental Needs Trust Rules

- Who should be the grantor?
 - Parent, another family member
 - NOT the disabled child
- Who should be the trustee?
 - Not the grantor or primary beneficiary
- Age of primary beneficiary: under 65
 - If beneficiary over 65, only option is pooled trust or, if not on needs-based benefits, direct transfer
- All primary beneficiaries must be blind or disabled
 - On SSI or Medicaid, or disability determination by MassHealth
- Trust must be irrevocable at date of funding
- Trustee discretion: beneficiary cannot demand income or principal
- Payback provision [(d)(4)(a) Trust] ?
 - NO, if trust created with parent's funds (Third Party Trust vs. Self-settled Trust)



Trustee/Trust safety valves

- Trustee limited power to amend
- Power to use trust assets to defend trust
- Authority to consume assets for primary beneficiary

- Minefields
 - Domicile of primary beneficiary could affect whether trust considered irrevocable
 - Make sure primary beneficiary does not contribute his/her own funds to the trust
 - Give trustee authority to fund a pre-need funeral for the primary beneficiary (also, authority to pay fees for professional advisors)
 - Make sure primary beneficiary cannot serve as trustee under any circumstances
 - Look out for reversionary interests hidden in boilerplate
 - Trustee powers, termination clauses, etc...

- Stick to the script – don't get creative



Administration of Special Needs Trust

- Trustee should not give cash to beneficiary if SSI is an issue
- Direct payments for food and shelter items reduce primary beneficiary's SSI benefit by 1/3 in month of payment (in-kind support and maintenance)
- Goods and services other than food and shelter allowed: medical care, house cleaning, insurance, computer and electronic equipment (less than \$3,000 value), furniture, vacations, etc.
- Beneficiary's funds must not be added to trust funds



Tax treatment of Special Needs Trust

- For grantor:
 - Gift tax: Not a present interest
- For beneficiary:
 - Income tax:
 - Complex trust - income can be accumulated
 - Deduction for distributable net income
 - Distributions to or on behalf of beneficiary taxed at beneficiary's rate
 - Grantor trust?
 - Giving grantor or beneficiary powers (IRC s 673-5) likely run afoul of benefits programs
 - Estate tax:
 - No general power of appointment – not taxable in beneficiary's estate



Personal Care Contracts

- What goes into a personal care contract
 - Services, payment, term
- Care in community vs. nursing home
 - MassHealth arguments:
 - Duplicates nursing home services
 - Unenforceable
 - Child provided services for free in past
- Viable planning tool?
 - Timing is everything
 - Pay as you go, if possible
 - If lump sum payment, provide reimbursement to elder's probate estate
- Stay tuned, litigation to follow



Reverse Half a Loaf

- The Theory
 - “Traditional” half a loaf (pre-DRA) = gift part, retain part to pay nursing home during disqualification period
 - Example: Elder in facility with \$78,800 in countable assets. He can keep \$2,000, so \$76,800 is “excess.” Net cost of care is \$7,680 a month
 - Elder could gift \$38,400 to child (1/2 of \$76,800) – disqualification period approximately 5 months (\$38,400 divided by \$7,680)
 - Elder retains remaining \$38,400 to pay facility during the 5-month transfer penalty period
 - Reverse half a loaf: gift all but \$2,000, donees “cure” portion of gift by paying elder’s medical bills until the disqualification period is equal to or less than the payout period



Reverse Half a Loaf, cont'd

- The Math (same facts)
 - Elder in facility gifts \$76,800 to child, retains \$2,000.
 - Penalty period: approximately 10 months [$\$76,800$ divided by $\$7,680$ (average cost of nursing home care)]
 - Child pays \$7,680 each month to facility from gift
 - In 5 months, child pays \$38,400 for nursing home (the Cure), leaving a net gift of \$38,400 to child
 - Net transfer penalty period after Cure, approximately 5 months ($\$38,400$ divided by $\$7,680$)
 - Theoretical result: Elder qualifies for benefits in 5 months



Reverse Half-a-Loaf: Viable Planning Tool?

- Why Reverse Half a Loaf Doesn't Work (post-DRA)
 - Disqualification trigger is not date at which elder is in the nursing home and down to \$2,000, but date at which no other funds are being used to pay for elder's nursing home care
 - During period when donee pays for elder's care, transfer penalty is not running out.
 - In previous example, trigger date for penalty period would be 5 months from transfer date
 - Is MassHealth policy tougher than federal law or a reasonable interpretation of federal law?
- Timing – community vs. nursing home
- May work in other states



Appeals

- Litigation, the final frontier
 - Personal care contracts: a contract is not a contract
 - Promissory notes: a note is not a note
 - Reverse Half a loaf
 - Rental property: if you have the assets you don't need the income
 - Annuities: MassHealth is a pessimist when it comes to life expectancy

DON'T TAKE NO FOR AN ANSWER