MEDICAID AND NURSING HOMES: PLANNING TECHNIQUES

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I. Introduction

Nursing home care is expensive. The costs deplete resources in a hurry. Oftentimes the nursing home resident, motivated to leave something for his loved ones, wishes to transfer his wealth to his family. If married, a nursing home resident may be concerned that his spouse will be impoverished by these costs. Regardless of the motivation, it is prudent for nursing home residents and their families to understand the circumstances under which Medicaid, a governmental program, would pay for nursing home care.

The federal and state governments fund Medicaid and determine eligibility for the program. The rules are complex. This article assumes the reader is familiar with these regulations in the nursing home context. I recommend that you read the companion article, Medicaid and Nursing Homes: An Introduction, on our website[2] if you are not already well versed with Medicaid rules. That article introduces key related topics as well, such as paying for nursing home costs, managing the family dynamics, and understanding the legal instruments that normally apply in these situations.

This article discusses some of the planning techniques I use in my practice in Tipp City, Ohio. It is not an exhaustive analysis of Medicaid or even how the program applies in this context. Because not all states run Medicaid the same way, and not all legal instruments function the same throughout the country, this article will be of most benefit for Ohio cases. Even though this article is not intended, and should not be construed, as legal advice for anyone, this is especially true for those situations that do not involve Ohio. Instead, I write this to promote understanding of the main considerations for over 90% of the cases I encounter in my practice.

My philosophy is to take full advantage of Medicaid benefits when this advances my client's goals.[3] I do not advocate what I consider to be risky or cutting edge strategies. There is not much room for this because the rules tend to make ineligible those who try to take unfair advantage of the program. More importantly, families in these situations already face challenging issues. I try to provide techniques that are conservative, effective, and likely to avoid a determination of ineligibility. If the reader is looking for the latest and greatest fad to try to abuse Medicaid, then this article is not for you.

II. Establishing the Foundation

A. *Clarification of Goals*

My first job as an attorney is to identify my client. In nearly all cases, this is the person entering the nursing home and his spouse. Just like one cannot use a map unless one knows the final destination, my initial priority is to understand what the client wishes to accomplish. This may be more easily said than done. Frequently, the nursing home resident, his spouse, and the family approach things as a unit and are scared and confused. Identifying my client can be a first step towards providing some clarity.

To determine my client's goals, I must effectively communicate with him. Sometimes the genuine objectives of the client come through immediately. Sometimes, especially if family discord or greed is strong, these are not so clear. Occasionally, I insist on a meeting alone with the client to try to filter out influences that compete with my client's goals, but most of the time this is not necessary.

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[3] I address the moral and ethical element of this philosophy in the companion article.

In the vast majority of cases, the client's goal is to preserve wealth in the family, to adequately provide for the spouse who remains at home (Community Spouse), or some combination of these two objectives. Of course, we must discuss an objective that is not necessarily a goal: paying for the cost of the care. This is in the best interest of the nursing home resident even though it is not always necessarily his wish.

B. *Inventory/Establish the Appropriate Legal Instruments*

Once I identify my client and ascertain his goals, I then obtain and review the basic legal documents. These are the Will, Financial Power of Attorney, Health Care Power of Attorney, and Living Will. Some or all of these documents may not be in place. Many times my client or a family member wants to just discuss Medicaid, or to get just one, but not all, of the documents, and they do not wish to consider how they will pay for the care, leave a legacy, or provide for the surviving spouse. These are important considerations that should not be ignored.

In this context, we are nearing the end of a life. It is prudent to consider who will make decisions when the nursing home resident is no longer able to do so. The potential impact of prolonged unconsciousness or imminent death could be significant. Addressing who gets what when death arrives is appropriate, too. If the proper instruments are not in place to address these issues, then just focusing on Medicaid can, so to speak, miss the train coming down the tracks. Just as the Karen Ann Quinlin and Terri Schiavo cases demonstrate, how and whether to end a life can become the most important issue of all. It is best to address all of these subjects, and make certain all of the legal instruments are in place, before moving on to Medicaid planning.

III. Determining Resources, Income, and Expenses

A. *Nailing Down the Numbers*

Once we have clear goals and the appropriate documents, we can then move on to considering what to do with specific assets. We must understand the nature and extent of all of the nursing home resident's resources, as well as his income and expenses, to determine what actions may be appropriate for particular items.

There is danger in not knowing the full parameters of these matters. One must identify current expenses, and how they may change, and ascertain the extent to which the income can meet these expenses, before one can gauge how long the income and total assets may pay for a person's nursing home costs. Moreover, all assets have particular characteristics and tax attributes that impact their suitability for Medicaid planning. For example, a sale or gift of a personal residence, certificate of deposit, savings or checking account, IRA, annuity, life insurance, stocks, and bonds all have different ramifications under Medicaid rules and the tax code. A planner must know exactly what a person owns, and whether he owns it outright or with another person, in order to give good advice.

B. *Income*

The nursing home resident must use virtually all of his income towards his care before Medicaid pays the remaining expenses. Permissible expenses for the nursing home resident are current and past medical bills, and health insurance premiums for himself, the Community Spouse, and his children younger than 18.

One should determine if taxes are being withheld and whether the person receives Medicare Part A or B benefits. If there are withholdings for taxes, then an analysis should be made to determine whether this is appropriate. Almost always it will no

longer be necessary to make withholdings for federal taxes because the deductions available from the nursing home costs will offset the income so that taxes will no longer be owed.[4] Further, the nursing home resident is well advised to have Medicare Parts A and B benefits and not just one or the other. Significant health care costs may not be covered if either coverage is absent. Federal retirees may not have Medicare A and B coverage.

For these reasons, I prefer to see an itemization of the gross income and withholdings of the nursing home resident and his spouse. For social security, this information appears on the 1099 SSA and with the annual notice of the amount of the cost of living increase. For pensions and annuities, this appears on the 1099 R and, quite often, on the stub for monthly checks that come in the mail.

If the nursing home resident is married, then it is important to determine both his income and that of the Community Spouse. Medicaid will not require the Community Spouse to pay any of her income towards the nursing home resident's care. Only the nursing home resident's income must be applied towards these costs. Prior to applying for Medicaid, the applicant should identify and segregate all sources of income to insure that none of the income of the Community Spouse is spent towards the nursing home expenses. Furthermore, the Community Spouse may receive a minimum amount of income each month known as a Monthly Income Allowance. To determine this amount, the Medicaid caseworker must be aware of the income each of the couple receives.

[4] Nursing home costs are deductible medical expenses so long as the person is there due to a physical condition and the availability of medical care is a primary reason for the residence. 26 USC §213(d)(1)(C) and 26 USC §7702B(c); 2007 U.S. Master Tax Guide, Paragraph 1016, at 355 (CCH 2006)(2007 US Master Tax Guide).

On a related note, health insurance premiums for both spouses are permissible expenses for the nursing home resident. If the Community Spouse provides the Medicare co-pay insurance, then the couple should explore the possibility of the nursing home resident obtaining and paying for this coverage. This could free up some income for the Community Spouse. In addition, consideration should be given as to how the Community Spouse will obtain her own coverage in the event of the death of the nursing home resident.

C. *Expenses*

A similar level of thoroughness should be given to the expenses. This is a moving target. No one spends the same exact amount each month. If the person is not yet in a nursing home, then they may be on the verge of substantial new expenses. Not only would this include the cost of the custodial care, but expenditures for prescription medicines can be significant, too. In one case my client had 15 prescriptions. Because the costs for medicines can vary greatly, these should be determined with some accuracy. To account for expenses incurred just once or twice a year, such as insurance for the home or automobile, I normally ask the client to account for all traceable expenses for the immediate six month period. Then we anticipate how this will change in the future.

A long term nursing home stay, as a major lifestyle change, affects the established patterns of expense. This does not begin and end with the costs for nursing home care and prescription medicines. Due to the institutionalization, travel plans change. With the focus on nursing home payments, gifts may be curtailed. Automobile expenses could dramatically decrease or increase. If unmarried, the nursing home resident usually will not need a car. The family may take the individual to doctor visits or the nursing home

could arrange transportation. On the other hand, the Community Spouse may wish to buy a new car or obtain a handicap accessible van. Both of these are exempt assets. Further, a Community Spouse may not wish to stay in the home. Instead, she may wish to sell it and downsize. Careful consideration must be given as to how lives may change so that the nature and extent of expenses can be forecast with some accuracy.

D. *The Burn Rate*

Once we determine the monthly expenses of the nursing home resident and Community Spouse, I compare this to the monthly income to calculate what I refer to as the "Burn Rate." This is the rate at which expenses exceed income. For example, if the nursing home resident and Community Spouse have monthly expenses of $8000 and income of $2500, then the Burn Rate is $5500 per month. Because the expenses could change, it may be appropriate to determine more than one Burn Rate.

E. *Assets*

Determining assets, in my experience, usually takes some effort. Let's touch upon the simpler tasks first. Although home appraisals by seniors are infrequent, the county auditor has a current value. As explained later, this particular value is of special relevance in Medicaid planning.[5] Obtaining it is important, but easy. A visit to the appropriate web site or a single phone call can retrieve it. Banks and brokerage houses send monthly or quarterly statements, so if we find a recent version this is normally sufficient.

Even the best organized folks, though, may not have all that we need. Most persons keep many of the relevant documents, but not all of them. Memories must be

[5] See the discussion on the Personal Residence at Page 31.

probed to see what is missing. Deeper digging through older files and boxes may be necessary. Some assets, like insurance policies and annuities, may only provide an annual statement. Oftentimes the most recent one cannot be located or it is several months or years out of date. We may have to contact the company, with a signed release, to gather this data.

However, a large percentage of the time, this exercise is even more challenging. Due consideration must be given to the sensitivities of an older person that has let their financial affairs slide into disarray, but diligence is mandatory. If we do not know enough about the assets, then the planning will suffer.

The biggest hurdles come from documents that are unorganized or non-existent. Because most parents do not fully share their financial data with their children, we often face the problem of the nursing home resident being forgetful and guarded, thereby complicating the task of figuring out just what they own. Sometimes the home has a collection of years of scattered papers. I have seen children gather full garbage bags of documents from their parents' house about assets that may or may not still exist. It can take weeks or months to go through dozens, if not hundreds, of documents and contact the institutions to learn whether or not the parent owns a resource with that company. If the parent still filed income tax returns, then this can provide clues and make the chore easier, but a large percentage of senior citizens no longer face this requirement or failed to file for several years. The task can be complicated if the Community Spouse is also forgetful or resents sharing this data with the children. Oftentimes folks forget what they owned and get statements on an irregular basis. Gas and mineral interests, assets held overseas, and partial interests in real estate for which the tax bill goes to someone else,

can be especially problematic. Nevertheless, if the client wants the appropriate planning, then someone must soldier through this process.

F. *Long Term Health Care Insurance*

Early in the case, I discuss with the client whether they have long term health care insurance (LTHC). If the nursing home resident has this coverage, then it dramatically affects our planning for the better. This provides a source of funds to pay the nursing home costs. It may also pay for assisted living or care at home and delay institutionalization. It is, by far, the best means for addressing the cost of custodial care because it does not force the nursing home resident to deplete his resources to the same extent that he must if the coverage is not in place. If the nursing home resident has this protection, then there may be no need to seek Medicaid coverage. If the LTHC benefits are meager and utilization of Medicaid remains a goal, then we could still utilize any of the planning tools as necessary.

If the potential nursing home resident does not have LTHC, then if he has the necessary level of mental or physical deterioration to qualify for Medicaid benefits, then he will not be able to obtain LTHC. No insurer would issue such a policy under those conditions.

It is not too late, though, to consider obtaining LTHC for the Community Spouse. This is a good time to explore the possibility. I encourage all of my Community Spouse clients to acquire it in these circumstances. It is widely available from many insurance agents in our area.

G. *Distilling the Income, Expenses, and Assets*

Once the assets, income, and expenses are sufficiently understood, we can then determine the Burn Rate and how quickly this will dissipate the total assets. If there is a monthly Burn Rate of $5000, then planning is much different for a nursing home resident with total assets of $50,000 versus $500,000. Moreover, planning is much different for a nursing home resident who owns a home versus one who rents or lives with family. Likewise, persons with the same level of assets may need different plans due to the tax consequences of sales or gifts. Only when we have a firm understanding about all of the assets can we prudently put together a plan. The rest of this article covers the Medicaid planning techniques that I most frequently use.

IV. Considerations for Married Couples and Individuals

Once we have a firm grasp of the income, expenses, and assets, and maximizing Medicaid benefits is a client goal, there are planning techniques that a nursing home resident, and his spouse, if he is married, should consider. These involve assessing the level of care required; prepaying funerals; acquisition of household goods and personal effects; buying or selling motor vehicles; use of personal service agreements; and prioritizing the liquidation of assets.

A. *Determining the Level of Care*

Even though a person may have mental or physical deterioration sufficient to qualify for Medicaid, institutionalization in a nursing home may not be desirable or necessary. Perhaps some extra help at home, or utilization of a day care facility, would provide the level of assistance necessary. Hiring a cleaning service, obtaining Meals on

Wheels, or regular visits to a senior center may fit within the existing budget and stave off the need for nursing home care. Even those who are Medicaid eligible may receive in home services through the Passport program and avoid institutionalization.

If independent living, by which I mean remaining at home, is not an option, then assisted living is a less intensive, less expensive step than nursing home care. Assisted living would typically consist of frequent monitoring, and limited assistance with ADLs, without the continuous oversight that one finds in a nursing home. This may or may not consist of board or cleaning services. The monthly cost for assisted living in the Tipp City, Ohio area in 2007 ranges from $2500 to $4500 per month, depending on the frequency and intensity of services provided. Although this requires relocation to a facility, the resident retains a greater level of independence and privacy than he would in a nursing home. It is also possible for married couples to room together.

Assisted living, or remaining at home with extra help, are less expensive and less radical changes of lifestyle than placement in a nursing home. These alternatives to full custodial care should be fully considered with the appropriate professionals. Obtaining an assessment from nursing home or assisted living staff is normally at no cost or very inexpensive. These professionals are willing to spend a few hours with a potential resident and family even though they may not receive a placement. If a person has a less restrictive and less expensive alternative, then they will be less likely to remain in a nursing home or assisted living facility for an extended period. Frequent turnover is expensive for institutions and they wish to avoid it. Because the assessment would be of little or no expense, and the professionals have a strong incentive to provide honest and

appropriate advice, it makes sense to fully explore the level of care required for the person in question.

B. *Pre-Paying Funerals*

Pre-paying funerals and related expenses is appropriate for four reasons. First, it gets out of the way a lot of decision making and painful choices that are difficult in the immediate aftermath of the loss of a loved one. Second, pre-paid funerals, plots, markers, and related items are exempt assets for Medicaid purposes. Third, purchase of the items now locks in the expenditure at today's rates. This avoids the cost of inflation. Fourth, it ensures that resources are available to take care of the funeral and related expenses. If the resources are not applied towards this cost now, then the money may not be available in the future from the decedent. The family may then have to bear these costs. Pre-paid funerals are funded by life insurance policies and heavily regulated by the states, so they are a reasonably safe investment.

C. *Household Goods and Personal Effects*

Under the Medicaid rules, household goods and personal effects of a reasonable amount are exempt. Replacing old and worn out items, or acquiring a new gadget, can add a pleasant sparkle to life. One can fill a home or a small nursing home room with new items and make an unpleasant change of life much more bearable. New clothes, shoes, dentures, glasses, hearing devices, a motorized scooter, and similar items can greatly improve the quality of life. A new television, computer, appliances, or furniture can stir attention, make snacks or juices more accessible, and spruce up the surroundings.

D. *Automobiles*

The general rule of thumb on motor vehicles is that an unmarried nursing home resident would typically shed this expense, while a Community Spouse should consider upgrading her transportation. A single nursing home resident usually will not be able to take extended trips. Off site visits are infrequent and short, such as consultations with doctors or a special family get-together. The exception would be a nursing home resident who wishes to have a handicap accessible van for these purposes, but this would be rare. A Community Spouse who still drives should consider buying a new vehicle if the existing transportation is aged. Further, the Community Spouse is much more likely to wish to have a handicap accessible van so that the couple could enjoy more fully, or have greater ease with, their off site trips together. Frequently we see couples that own more than one vehicle. Consideration should be given to owning a single, well functioning car to reduce expenses and the flow of documents related to motor vehicles, such as insurance statements and registration notices.

E. *Personal Service Agreements*

Some family members spend significant time caring for a parent or other relative. It is not unusual for us to see a son or daughter spend fifty to one hundred hours per month, or more, with the parent or addressing their affairs. Usually the care is given without notice and on weekends and holidays. To hire this type of service from a business could cost several thousand dollars per month.

More often than not, the family member who gives this service receives no payment. Love and affection motivates them. However, they do not necessarily have to provide their services for free.

Ohio recognizes an express agreement to pay for personal services by one family member for another if the arrangement is proven by clear and convincing evidence.[6] Therefore, if there is a written fee agreement between the caregiver and recipient, then payments for these services, as long as they are reasonable, should be enforceable and not be treated as gifts by a Medicaid caseworker.

Although these contracts can be simple and effective, a number of consequences flow from their use. From a tax perspective, there is much less paperwork if the caregiver serves as an independent contractor. This eliminates the need to prepare and file payroll tax reports. If the caregiver receives more than $599 in a year, then the payor must issue a 1099. This is a lot less challenging than dealing with payroll tax returns. The recipient must pay regular income taxes, as well as Social Security and Medicare taxes, upon this income. Of course, payment of the nursing home resident's funds towards custodial care is really a 100% tax, which is significantly greater than the taxes triggered by this type of arrangement. Nevertheless, everyone involved in the transaction must understand the income tax requirements and prepare to meet their obligations.

There are non-tax considerations, too. The caregiver should check his auto insurance policy to make certain that he retains full coverage in the event he causes an accident while performing tasks under the personal services agreement. Technically, an insurer may interpret this as a "hired auto" type of exemption from coverage. A quick call to the insurance agent for clarification, or to get an endorsement to the policy, would be in order.

[6] Merrick v. Ditzler, 91 Ohio St. 256 (1915).

In addition, the caregiver should have his own health, disability, and life insurance in case he becomes injured in the line of duty. With a written independent contractor agreement like this, normally workers' compensation benefits would be denied. If the caregiver has her own life, health, and disability coverage, then there should be no need to file a claim.

Because these issues can be resolved with careful planning, personal service agreements can compensate the caregiver, legally reduce the nursing home resident's resources, and prudently cover the responsibilities and risks. Payment for personal services is not a permitted expenditure for a Medicaid recipient, so use of these agreements would only be applicable prior to the nursing home resident's receipt of Medicaid benefits or to assist the Community Spouse. Although legitimate use of a personal service agreement would not cause a large expenditure each month, over time it could move a significant amount of wealth from the recipient of the services to the caregiver.

F. *Prioritizing the Liquation of Assets*

Payment of significant nursing home costs will normally require the liquidation of investments. Few persons keep enough cash in their checking and savings accounts to cover more than a few months of the expense. Eventually one must decide the order in which assets should be converted to cash to pay for the costs.

There are many types of assets, but this article will consider the consequences of liquidating those resources a senior citizen is most likely to have. These are real estate, Roth IRAs, traditional IRAs, Series "E" U. S. savings bonds, mutual funds, stocks and bonds, life insurance, annuities, and certificates of deposit (CDs).

The main consideration in these circumstances is the income tax consequence. As already discussed, in all likelihood the nursing home costs will produce sufficient tax deductions so that the nursing home resident and his spouse will have little, if any, income tax to pay.[7] This is based on the assumption that the nursing home resident and his spouse have pension and other income each year that totals less than the annual nursing home expenses. This further assumes that the nursing home resident and spouse would not sell substantially more of their investments than necessary to pay for the care as these expenses are incurred.

Before proceeding, we should explore the concept of "basis" under the federal income tax code.[8] By "basis" I mean the value of an item for purposes of determining a profit or loss upon its sale. For example, if a person pays $40 for a stock, then sells it for $100, the basis would be $40. Because the sale price exceeded the basis by $60, the person would have to pay capital gains taxes on $60.

When a person makes a gift during his life, the recipient of the gift receives the donor's basis in the property. To continue the above example, if a person pays $40 for a stock, then gives it to his child, then his son or daughter will have a $40 basis in the stock. Commentators refer to this as a "carry over" in basis.[9]

On the other hand, if a parent dies owning a $40 stock that has increased in value, then the son or daughter inheriting it receives a "step-up" in basis to the fair market value at the parent's death. Thus, if the parent paid $40 for a stock that increased in value to $100 at his death, then the son or daughter would have a basis of $100 in that same stock.

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[7] See footnote 4 at Page 6.
[8] For a thorough, well annotated discussion of basis, see Chapter 16 of the 2007 US Master Tax Guide.
[9] If the donee sells the stock at a loss, the basis would be the lower of the donor's basis or the fair market value at the time of the gift.

If the child then sold it for $100, then they would pay no capital gains tax upon the sale. Therefore, there is an income tax advantage for the son or daughter to inherit property with a low basis from a parent instead of receiving it as a gift.

In addition to basis, there are a few other tax concepts of which the reader should be aware. Nearly all traditional IRAs have a basis of $0.00.[10] This is because a traditional IRA normally consists of funds rolled over from a 401(k) or 403(b) plan at work, or the account holder deducted the IRA contributions on his income tax return. As a result, no income taxes were paid on this money. Consequently, once the funds are taken out, they will count as taxable income during the year of withdrawal.

Roth IRAs work differently than traditional IRAs.[11] The main attraction of a Roth IRA is that if the funds remain invested for five or more years, then the original investor who has reached age 59 1/2, or his beneficiary upon his death, will pay no income taxes on the withdrawals.

An asset that normally has a low basis is a U. S. Savings Bond, Series "E." These accumulate interest, sometimes for decades, that is finally payable when the bond is surrendered.[12] It is not unusual for bonds that originally cost a few hundred dollars to increase in value to several thousand dollars. The owner of the bond must report the accumulated interest as taxable income when the bonds are cashed in. If the purchaser dies owning the bonds, then they must be surrendered at that time.

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[10] For a thorough, well annotated discussion of traditional IRAs, see Paragraphs 2168 through 2179, Pages 647 to 654, of the 2007 US Master Tax Guide.

[11] For a thorough, well annotated discussion of Roth IRAs, see Paragraphs 2180 through 2180G, Pages 655 to 658, of the 2007 US Master Tax Guide.

[12] The interest on "E" bonds must be declared and paid each year for accrual basis taxpayers, or it may be deferred by trading them for "H" bonds. It would be rare, though, for a potential Medicaid recipient to be on the accrual rather than the cash basis. See Paragraph 730, Page 258, in the 2007 US Master Tax Guide.

Based on these tax rules, it is prudent to consider liquidating the traditional IRAs, then U. S. "E" Savings Bonds, before turning to other assets. In most cases the nursing home costs generate significant tax deductions that the children do not have. If the parent realizes the income from the traditional IRA, then nearly always he would pay less federal income tax on the proceeds than a child that receives these funds via a rollover.[13] Further, the "E" Bonds will have to be surrendered no later than the owner's death, thereby causing the decedent to receive this as income. Once again, the owner's nursing home costs should cause significant deductions to offset some, or all of, the interest income.

If the nursing home resident does not have a traditional IRA or "E" Bonds, then their resources may consist of a Roth IRA, real estate, mutual funds, stocks and bonds, annuities, and life insurance. The Roth IRA, if more than five years old, would be one of the last assets to liquidate because of its high basis. For the real estate, mutual funds, and stocks and bonds, one should compare the basis of the asset with its current fair market value. Generally, one should consider selling first those assets for which the basis is lowest and the gain would be the highest. The nursing home resident and spouse usually have sufficient tax deductions to diminish, if not eliminate, capital gains taxes from the sale of most assets. However, one should analyze the facts before a sale. If the gain would be large enough so the parent would pay taxes, then delaying the sale could be the smart choice. It makes sense to avoid paying taxes as long as possible. If the decedent dies shortly after an asset is sold, then it would have been best to sell the asset with the least amount of taxable gain. This would permit the children to inherit assets that receive

[13] A non-spouse traditional IRA beneficiary may roll over the IRA into an "inherited IRA" and defer the tax in some situations. See Paragraph 2177, Page 652, 2007 US Master Tax Guide.

a step-up in basis to the fair market value, thereby putting the surviving beneficiaries in the best possible income tax situation.

Life insurance, annuities, and CDs have some attributes that merit special attention.

There are two types of life insurance: whole and term. Both types pay benefits when the insured dies. In nearly all cases, death proceeds from life insurance are not subject to income tax. In addition, whole life policies have a cash surrender value that can be obtained by borrowing against or surrendering the policy during the owner's lifetime.[14] Once the policy is borrowed against or cashed in, the death benefits are reduced or eliminated. Term policies have no cash surrender value.

If the death benefit of a whole life policy is significantly greater than its cash surrender value, then it is advisable to avoid cashing in the policy. Of course, if the policy has significant premiums, then this must be taken into account. Due to the nursing home costs, the nursing home resident may not be able to pay them. One often finds, though, that life insurance policies owned by senior citizens have a cash surrender value that is quite close to the death benefits. In these cases, it may be advantageous to surrender the policy. It would not be prudent to continue making payments on a life insurance policy that will not increase in value.

Normally, if premiums are still payable, then term insurance on older persons is quite expensive. Oftentimes the cost of the coverage in a year or two will exceed the death benefits. If so, then a sober analysis should be made of the life expectancy of the

[14] This article assumes the whole life policy is a simple one the nursing home resident or spouse acquired from a non-business setting and the basis meets or exceeds the cash surrender value. If this is not the case, then this analysis may be wholly inappropriate. If the policy basis is significantly lower than the cash

insured versus the cost of the coverage during this time. If the amount invested is not likely to exceed the death benefits, then the policy should be permitted to lapse. On the other hand, if it appears appropriate to keep the term coverage, then consideration should be given to the choice of beneficiaries. As discussed later in this article, it may be prudent to make children the beneficiaries of the term policy instead of a spouse.[15]

Annuities do not receive a step-up in basis when the owner dies. Thus, there is no advantage to inheriting an annuity like there can be when one inherits real estate, mutual funds, or stocks and bonds. At the annuitant's death, the proceeds are payable to the beneficiaries listed in the agreement. Any earnings in the contract will be taxable income to the recipient regardless of whether they are payable at death or before this time. A percentage of each payment the owner or beneficiary receives is subject to income tax. When determining whether to cash in an annuity to pay for nursing home costs, one should compare the amount of earnings that would be subject to tax from doing this versus selling some other asset. From a tax perspective, there is no general rule as to when annuities are most suitable for paying nursing home costs.

However, annuities, like certificates of deposit, may charge a penalty for a premature surrender. Most annuities charge a surrender penalty of some sort within the first ten years of purchase. Sometimes these can be as much as 10% of the original price. A typical surrender charge may be 10% within 12 months of purchase, 9% the next year, and so on until it is just 1% in the tenth year after acquisition. If the surrender penalty is substantial enough, then it may be advisable to delay liquidation of an annuity and sell other assets first. Surrender penalties for certificates of deposit, which can be imposed at

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surrender value, or if there is any doubt as to the matter, then the company agent should be consulted before any action is taken with the policy.

any time, are usually much less severe than those that apply to annuities that are only a few years old. Some annuities and CDs waive the surrender charges if the owner dies. One must read the agreement to see whether this type of exception would apply.

V. Planning for Married Couples[16]

A. *Maximizing Exemptions, Generally*

There are some planning considerations that are unique for married couples when a long term nursing home stay is in the picture. Chief amongst these are maximizing the available exemptions and planning for the Community Spouse Resource Allowance (CSRA).

If the nursing home resident has a Community Spouse, then providing for her comfort and care is a prime consideration. Fully utilizing the Medicaid exemptions promotes this goal. We have already discussed the virtues of prepaying funerals, acquiring household goods and personal effects, and upgrading the motor vehicle, all of which are exempt assets in these circumstances.[17] The exempt asset that gains the most attention, though, is the personal residence.

B. *The Home Exemption*

As long as the Community Spouse remains at home, then this real estate is exempt, regardless of value, for Medicaid purposes. An obvious strategy is to acquire the most valuable real estate possible. As we discuss later in this article, if passing along a legacy to the children is a goal, then this may not be the best strategy in light of the

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[15] See the discussion on recoupment of Medicaid benefits starting at Page 26.

[16] A recent development in a handful of states is civil unions or marriage by gay couples. I have not done Medicaid planning in this context, but have some ideas on how I would go about it. However, this topic deserves its own article, so I will not explore it here.

State's powers of Medicaid recoupment, but it can lock up a lot of family wealth and save it from immediate expenditure on nursing home costs.[18]

Taking advantage of the home exemption can take two forms: the first is to acquire a different residence. The second is to improve the existing premises. Regardless of the approach selected, use of the couple's resources to buy a new home or fix up the old one is permissible. Perhaps a whole new setting is desired. Acquiring a new home could fill this need. Perhaps fixing up the existing residence would be more appropriate. If so, then installing wheelchair ramps, widening doorways and halls, and making bathrooms more user friendly could meet the more immediate needs. Other improvements to the existing home could include new windows, heating and cooling equipment, a roof, water heater, upgrading the electric and plumbing, and replacing a dirt driveway with a concrete or asphalt version.

C. *Community Spouse Resource Allowance*

The Community Spouse Resource Allowance (CSRA) is the amount of non-exempt assets Medicaid will permit the Community Spouse to keep even though the other spouse is a nursing home resident who receives Medicaid. The minimum CSRA is $20,328, while the maximum is $101,640.[19] Medicaid determines the CSRA by looking at all of the couple's assets, excluding those that are exempt, then adding up everything that remains. If the total remainder is less than $40,656 then the Community Spouse may keep $20,328. If the non-exempt assets are greater than $40,656, then the CSRA equals half of the non-exempt resources or $101,640, whichever amount is less.

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[17] See the discussion earlier in this article at starting at Page 13.
[18] The discussion on Medicaid recoupment starts later in this article at Page 26.
[19] These amounts are effective as of January 1, 2007.

A unique feature in determining the CSRA is the treatment of debts. Medicaid does not take unsecured debt, like credit cards, into consideration.[20] Secured debts, like a house mortgage or car loan, normally secure an exempt asset, like the personal residence or an automobile, so they are not taken into account in most cases, either.

Even though this treatment of debts defies common sense, it is important to be aware of it and plan accordingly. The CSRA is determined as of the first month of continuous institutionalization of the nursing home resident. The couple should avoid making large reductions of debt prior to this time. This will reduce the pool of assets and diminish the size of the CSRA. Some commentators state that to increase the size of the CSRA, the couple could take out a loan, thereby increasing their gross assets, and then pay off this debt once Medicaid determines the CSRA.[21] This is a logical suggestion that I have made to many clients. As a practical matter, I have not yet met a couple in these circumstances that is willing to do this. Acquiring new debt is too contrary to the inclinations of most senior citizens.

If the couple's non-exempt assets are greater than $203,280, then the largest CSRA the Community Spouse may receive is $101,640. The nursing home resident shall not be eligible for Medicaid until they spend down to the $101,640 level. This excess amount must be spent for the sole benefit of the couple, on their legal obligations, or to acquire and maintain exempt assets. Once the CSRA is determined, it would be appropriate, at that time, to pay debts. If the funerals have not already been purchased, then now would be a good time to do so. Buying other exempt assets, such as household

[20] Medicaid permits the institutionalized spouse to pay medical bills for himself and the family from his income, but this, in a technical sense, is unrelated to the CSRA. For authority that unsecured debts are not taken into consideration, see Gregory S. French, Ruth R. Longenecker, and Richard T. Taps, Ohio Elder Law Practice Manual, at 112-113 (2006).

goods and furnishings, an automobile, a handicap accessible van, or improving the residence or acquiring a new one all merit consideration. Any purchase that is not a gift for someone else is a permissible expense. It would be perfectly legal for the couple to buy frivolous things like lottery tickets. Perhaps the Community Spouse could take a long delayed trip or purchase a nice piece of artwork she has always wanted. Although some acquisitions are more sensible than others, if the couple does not spend the excess on themselves, then they will have to spend it towards nursing home costs in order to reach the CSRA level and obtain Medicaid benefits.

Once the caseworker determines the CSRA, the couple has twelve months to place the assets that comprise the CSRA into the sole name of the Community Spouse. Care should be given in the selection of these assets. The same criteria used to determine the prioritization of the liquidation of assets would also be applicable here. For tax reasons, it would be sensible to liquidate assets with no or a low basis, such as traditional IRAs and savings bonds, as needed to pay the nursing home costs and spend down to the CSRA. The CSRA, ideally, should have the remaining assets with a higher tax basis.

D. *Separation or Termination of the Marriage*

Separation, or termination of the marriage, could be a powerful planning tool, but I have never seen it employed. Beginning the month after separation, the assets of the couple are no longer deemed available to each other.[22] If a couple quits living together, or if they keep cohabiting but end the marriage, then Medicaid would only consider the resources of the nursing home resident. I will not bother to analyze the possibilities this

[21] Ohio Elder Law Practice Manual, at 121.
[22] Ohio Administrative Code (OAC) §5101:1-39-34 (H)(1).

presents because, in eighteen years of practice, I have never encountered a couple willing to consider this option.

VI. Planning for Unmarried Persons.

A. *Generally*

The main consideration for unmarried persons who face a long stay in a nursing home is that Medicaid will only permit them to have $1500 of non-exempt assets. Once the appropriate exempt assets have been acquired, such as a pre-paid funeral, household goods and furnishings, and personal effects, the issue then becomes what to do with the remaining assets.

Payment of existing debts may or may not be in the best interest of the nursing home resident. If the person has a large debt load and few assets, then it may be in his best interest to pre-pay his funeral and acquire some exempt assets before he pays his other bills. Having new clothes, a hearing aid, dentures, or similar items, would mean a great deal to the nursing home resident, and paying for the funeral would spare the family this expense. Although it would short-change creditors, there may be little downside risk to the permanent nursing home resident. After all, he will not need a good credit rating, so unpaid bills are not of much concern. Further, he would be "judgment proof" in that a creditor would not be likely to seize his assets. The few items he owns would not be worth enough to justify the effort to take them.

B. *Confounding the Right of Recoupment*

If Medicaid pays the nursing home costs of a person aged 55 or older, then the State of Ohio has the right, upon that person's demise, to be paid back for the cost of his

care. Any assets the nursing home patient owned or controlled at his death are subject to this claim.

There are three types of instances in which this right of recoupment is most likely to arise. The first is when the Community Spouse survives a nursing home resident who received Medicaid. Although the State of Ohio is barred from seeking recovery while the surviving spouse lives, the State has the right to seek recoupment upon the death of the surviving spouse. The second is when the resident is unmarried and his only non-exempt asset is his home. Medicaid will, in most cases, go ahead and place the person on Medicaid, but require him to sell his residence and use the proceeds to pay for his care.[23] The third situation is when the nursing home resident on Medicaid owned assets of which no one was aware or he received an inheritance.

Many legal steps can make it difficult for Ohio to exercise its right of recoupment. All of these steps involve the conversion of probate assets into non-probate assets. By "probate" assets, I mean items in a decedent's name that are not automatically payable on his death to someone else. "Non-probate" assets are those that a decedent owns that are automatically payable on his death to someone else. Non-probate assets one normally encounters are those owned in a joint and survivorship fashion and transfer on death accounts.

Although Ohio has the right to gain recoupment from non-probate assets, it is very difficult to do so. If a Medicaid recipient dies and someone opens a probate estate for them, then this Executor or Administrator may receive a letter from the Ohio Attorney General notifying them of the recoupment claim. Although I have never confirmed this, I

[23] The exception to this rule is when the exempt home is worth more than $500,000. In that case, the person will not be eligible for Medicaid.

assume the initiation of a probate case in Ohio triggers a monitoring mechanism that the Ohio Attorney General has in place specifically for this purpose. As a result, whenever a probate estate is opened in Ohio, the Ohio Attorney General checks this with a database of recipients who have received Medicaid. Further, an Executor or Administrator opening an estate has the duty to inquire as to whether the decedent ever got Medicaid benefits.[24] If so, then the Executor or Administrator must send a notice to the State of Ohio informing them of this fact. This provides the State an opportunity to file its claim and seek payment.

However, a different set of circumstances arises with non-probate property. Oftentimes there are no probate proceedings when there are only non-probate assets. Thus, the State of Ohio may not know of the decedent's death. Further, the beneficiary of the non-probate property does not have a duty to notify the State that the decedent received Medicaid benefits. Accordingly, it is much more difficult for the State of Ohio to gain recoupment when a decedent's assets are owned in a non-probate form.

A legal and effective technique to confound the right of recoupment is for the unmarried person to own his or her assets in a non-probate fashion. If the single person wishes to increase the chances that he will pass his assets to his children, or other beneficiaries, instead of having them paid to satisfy the State's recoupment claim, then placing his assets in a non-probate form increases his chances of realizing his goal.

For real estate, an easy way to accomplish this is to utilize the transfer on death deed.[25] Having the owner transfer the property to himself and another person with joint and survivorship rights is another method to convert the home into a non-probate asset,

[24] Ohio Revised Code (ORC) §2117.061.

but it has some potential complications.[26] In those situations in which the unmarried nursing home resident receives Medicaid while waiting to sell his home, then transferring his real estate back to himself via a transfer on death deed is a viable option. Likewise, this same technique could be used by a surviving spouse of a deceased nursing home resident who received Medicaid. To obtain such a deed, hiring an attorney is necessary, but the cost of the instrument and recording fees should be less than $100 if the prior deed is available and the legal description is acceptable to the County Engineer.

For bank accounts, automobiles, stocks, bonds, and mutual funds, use of joint and survivor or transfer on death mechanisms to turn probate into non-probate property is easier than it is with real estate.[27] A short visit to the bank or broker for this purpose can usually switch over the account to the non-probate form. For automobile titles, if the vehicle does not have a loan outstanding, then signing over the old title in front of a notary, then taking it to the motor vehicle title office to obtain the new title, is all that will be required.[28]

C. *The Personal Residence*

No asset gets as much attention under the Medicaid rules as the personal residence. There are several alternatives for preserving this asset in the family.

Sometimes a son or daughter will move in with an elderly parent. If this child's care keeps the parent out of a nursing home for at least two years immediately before the entry, then the parent may give the residence to the child. It is not advisable to just

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[25] ORC §5302.22.

[26] It may result in a gift, requiring the filing of a gift tax return. This is discussed more thoroughly at Pages 45 to 46.

[27] The same tax complications that can arise by using joint and survivorship deeds to make real estate non-probate property can also arise with non-real estate types of property. See the discussion of basis at Pages 17 to 18, and the discussion of estate and gift taxes at Pages 46 to 47.

assume this standard is met. Instead, one should review the form Medicaid uses to make this determination. This is the JFS03697 "Level of Care Assessment." If possible, this form should be taken to a doctor who has cared for the parent for at least the last two years to learn his opinion. Although Medicaid will have its own investigator look into the facts, if the treating physician, after reviewing this form, states that the child's care kept the parent out of the nursing home for at least two years, then this is a good indicator that the transfer may be appropriate. In any event, it is prudent not to record such a deed of conveyance until Medicaid issues its ruling. If the caseworker maintains that the care did not meet the appropriate standard, then recording the deed could cause a gift that triggers an ineligibility to receive Medicaid.

Another note of caution is in order. The standard is that the child must reside with the parent. Visiting every day to make certain the parent is fine is not good enough. The child must actually take up residence in the parent's home. Regularly sleeping there, as well as consistently bathing, getting dressed, and eating in the home are important elements that should be met. Mail delivery or listing the address on a driver's license may not be sufficient. In addition, maintaining a separate residence could jeopardize the exemption.[29]

Although this exception arises quite infrequently, the home may be transferred to the nursing home resident's child who is blind, permanently and totally disabled, or under the age of 21. Such a transfer would not count as a gift that could cause Medicaid ineligibility. On a similar note, the home is not a countable resource if the individual's

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[28] If the car has a loan on it so the lender holds the title, then obtaining a new title could be difficult if not impossible.

[29] The following Medicaid state hearing decisions discuss these issues: Appeal No. 1032813 (Summit Co. 2001); Appeal No. 1001723 (Butler Co. 2001); Appeal No. 822960 (Trumbull Co. 1998).

child, age 65 or older, lives there and is financially dependent upon the nursing home resident.

Occasionally we encounter cases in which elderly siblings live together. If a sibling owns an interest in the residence and lived there for at least one year immediately prior to the other sibling's entry into a nursing home, then a transfer of such residence to this brother or sister is allowed. This equity of the healthier sibling must be a documented, legal interest. It is wise to obtain a copy of the recorded deed to confirm the ownership status. If all parties agree that the healthier sibling has such an interest, but there is no recorded deed to verify it, then the parties should put such a deed in place. For cases in which the deed would be signed and recorded just prior to or after nursing home placement, it would also be worthwhile to verify the source of the equity. Applicable instruments could include bank deposit slips, loan documents, closing statements, prior deeds, tax returns, property tax bills, or anything else that tends to prove the contribution.

If the home will be sold, then the Medicaid rules may operate so that anyone, including a family member, could purchase it for less than its true fair market value. Medicaid presumes that real estate is worth the appraised value listed by the local county auditor. Frequently, these valuations are less than fair market value. Consequently, this may present an opportunity for the home to be sold at a price lower than what it is really worth. In fact, if the owner of the residence is a nursing home resident who receives Medicaid while his home is for sale, then he may not refuse an offer that is equal to or greater than 90% of the county auditor's value.[30]

If a child has the financial ability to purchase his parent's home, then this presents an opportunity to acquire it at a favorable price. This could be part of a plan to preserve a

parent's ability to live there. Additional measures could be taken to give some protection from creditors and to share ownership amongst the children.[31]

VII. Gifting

A. *Risks*.

When confronted with the need to pay approximately $6000 a month for nursing home costs, the nursing home resident and his spouse may consider the option of giving assets to their children to save them from depletion by these expenses. Although it may be possible to make gifts and, eventually, gain Medicaid benefits, it is always a risky strategy.

The underlying assumption is that the gifting parent, headed to the nursing home for the rest of his life, will no longer need his money if Medicaid will pay for his care. This assumption may prove accurate, but there are so many problems with this logic, and the results could be so disastrous, that it is important to review the most likely things that could go wrong.

Before I set forth the risks and explain how gifting could be done, let me make clear: I do not recommend or advocate gifting in these circumstances. Nevertheless, one can legally do it. I provide advice how to do so because a person has the right to receive such guidance.

The nursing home resident must understand that they have no power to retrieve the money once it is given away. If the donor retains any interest in the property, then it may not count as a gift, and Medicaid could declare it available to pay for the costs of his

[30]OAC §5101:1-39-05(C)(6) and §5101:1-39-31.3(B)(4).
[31] I explain these techniques at Pages 42 to 45.

care. This would bar Medicaid eligibility. Consequently, to be effective, gifts must be completely unconditional. This means, under no circumstances, could the parent force the child to return the assets. Therefore, if the gift is unconditionally made, and the parent has improved health, cannot receive Medicaid, wishes to buy anything, or becomes displeased with the recipient of the gift, then there may be no way for the donor to retrieve the bequest.

Moreover, circumstances could change in the life of the person who receives the gift. Usually the assumption is if Mom or Dad needs the money, then the child will either return what is needed or use the gift to pay for whatever the parent requires. However, since the gift is unconditional, the child is not obliged to use it for his parent. The child could simply decide that he wishes to keep the money. There are other risks, too, such as debt problems, filing bankruptcy, ill health, dying and leaving the asset to others, selling the asset, a market crash or bank failure, divorcing, gambling the proceeds away, and so on. Just because a child is stable, in a long term marriage, has no debt problems, and has been in good health for decades is no guarantee of the future.

Another big risk is that the laws could change. Sound planning today could be disrupted by legislation tomorrow. This happened as recently as February 2006 when Congress made some of the biggest changes ever to the Medicaid rules.

Another risk that should be kept in mind is the hazard of making unequal gifts. Nothing is more likely to cause contention amongst the children than giving one more than another. Quarreling children can make the parent's last days unpleasant. They can go through the money by suing each other, they may quit seeing the parent, and they may become less inclined to be generous to their Mom or Dad who gave them the money in

the first place. If the parent wishes to make unequal gifts, or completely cut a child out of the process, then they are taking a big risk regardless of the circumstances.

Only if the potential donor is aware of all these risks and, nevertheless, is comfortable with them and wishes to proceed, should gifting be considered. Even if the parent is willing to part with some or all of his assets, the Medicaid rules are such that only some individuals should consider making gifts.

B. *Getting Past the Five Years*

Due to the five year look back period for gifts made on and after February 8, 2006, it is not advisable to make gifts unless funds will be available to pay for nursing home costs for the full five years after making them.[32] This is due to the manner in which the ineligibility period would apply.

Once the caseworker calculates the number of months of ineligibility, he then determines when it shall begin. It starts on the date an individual receives nursing home care and would otherwise be eligible for Medicaid coverage. For an unmarried individual, this would be the date he has no more than $1500 in non-exempt resources, is institutionalized, and meets all the other criteria such as citizenship and sufficient deterioration. For a married nursing home resident, this would be the date the couple has spent down to the CSRA and all of the other tests are met.

If a Medicaid application is submitted less than five years after a gift, then ineligibility could result that would stretch past these five years. For example, if the application is submitted in the 59th month after a gift, then ineligibility could last for several months or years that would have been avoided if the application would have been

delayed by another month. Therefore, it is crucial that the application not be made anytime within five years after making a gift.

Likewise, if the decision is made to make gifts, then it is important to do it immediately. Indecision and inertia can be costly enemies in this process. Every month of delay in completing the transfers means another month has passed without commencing the five year period. The goal is to reach the 61st month as rapidly as possible. Each month of inaction could, at today's rates, cost another $6000 in nursing home care that Medicaid may otherwise have covered.

Deciding how much to give should be analyzed in the setting of the five year look back period. If, five years after making gifts, the nursing home resident still has more than $1500, or the couple has more than the CSRA, then he would remain ineligible for Medicaid. Some persons may be unwilling to give everything away. This is understandable. Gifting, when one is encountering huge expenses, is contrary to common sense. However, if the donor gives away too little, then at the end of the five years he is still ineligible. Some persons are comfortable with this possibility and take the view that at least they were able to keep some assets in the family. One should consider this possibility at the beginning of the process. If some gifts are made, then there is a delay before giving away the remaining assets, then a lot could be spent on nursing home care that could have been paid by Medicaid if the whole enchilada had been swallowed at the beginning of the process.

Because of the dire consequences that could arise from the submittal of a premature application, it is crucial to analyze the amount of funds necessary to cover

[32] This analysis applies to gifts made on and after February 8, 2006. For gifts made before this date, there is a three year look back period and the ineligibility is tied to the date of the gift. Thus, for pre-February 2006

expenses during these five years. By multiplying the monthly Burn Rate times sixty months, the result is the amount of assets that should be available as a strategic reserve in the event they are needed. If there are not sufficient funds available to cover this strategic reserve, then it is inadvisable to make any gifts.

C. *Trusts*

If there are sufficient assets to fund this strategic reserve, then the next consideration is who will keep the money and how it could be made available.

Once again, we see that LTHC is an ideal planning tool. The insurance company, which is highly regulated and subject to solvency requirements, would supply the funds. If the benefits are large enough, then they could cover the entire cost of the nursing home care. This would remove the risk of depending on a son or daughter to maintain the assets and make them available for the parent's use. Even if the LTHC benefits could not pay all of the costs, then the more of the expense it could cover, the more of these risks it would remove.

Conceptually, using a trust to hold the strategic reserve would work well. Unfortunately, placement of the assets of the nursing home resident or his spouse into a trust could result in Medicaid deeming these resources available to pay for nursing home costs. Since this is the result the nursing home resident wants to avoid, it is important to know how this outcome could arise. This requires an understanding of some of the Medicaid rules on trusts.[33]

Of the five types of trusts recognized by Medicaid, one has the most potential to cause problems in this context. This is a "self-settled trust established on or after August

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gifts, the ineligibility period is either running right now or has expired.

[33] These are found in OAC §5101:1-39-27.1.

11, 1993." This trust has three characteristics.[34] First, the assets of an individual who applies for or receives Medicaid benefits form all or part of the trust. Second, the trust is not established by a will. Third, the trust is set up by the nursing home resident, his spouse, authorized agent, or by a person acting at the direction of or upon the request of the nursing home resident or his spouse.

Generally, any agreement is a trust if it is "an arrangement in which the grantor transfers property … with the intention that it be held, managed, or administered by a trustee for the benefit of the grantor or certain designated individuals (beneficiaries)."[35]

In the typical situation, the nursing home resident wants his children to take the assets he gives them and keep the resources for his benefit in case he needs them in the future. This type of understanding falls squarely into this rule. The money comes from the nursing home resident, the funds are distributed during his life without a will, and the children place the assets into some sort of arrangement for future use on behalf of the parent. Since the nursing home resident is the beneficiary of the arrangement, Medicaid would consider the assets available for the applicant's use. If there is more than $1500, then this bars eligibility for Medicaid.

Avoiding the use of a written instrument does not necessarily get around the problem. This is because the Medicaid rules consider a "legal instrument or device similar to a trust" to be the same thing as a trust.[36] Therefore, if there is an unwritten understanding to hold the funds on the nursing home patient's behalf in case he ever

[34] OAC §5101:1-39-27.1(C)(2)(a).
[35] OAC §5101:1-39-27.1(B)(13).
[36] OAC §5101:1-39-27.1(B)(7).

needs them, then there is a danger that Medicaid would deem the funds available for nursing home costs and deny benefits.

This author is not aware of any foolproof arrangement to permit the children to keep Mom or Dad's assets and "agree" to keep the funds for the nursing home patient's use in case he needs them. Any such arrangement runs the risk of coming within the Medicaid trust rules and causing the assets to be deemed available for the nursing home resident's use.

If the goal of the nursing home resident is to make gifts to children or close family members and to save these assets from nursing home costs, then he risks Medicaid ineligibility if there is any "agreement" or "understanding" that could make these funds available for his future use.

If the nursing home resident wants to make gifts to try to gain Medicaid eligibility, he must understand that there can be no strings attached to the gifts. Even a simple discussion as to what he would like to see his children do with the assets risks a finding that he gave the money with the intention necessary to create a trust.

What can be done to try to avoid a finding that gifts are part of a trust? As long as anyone holds assets for the nursing home resident's benefit “at the direction of or upon the request of the nursing home resident,” then a key element of the definition of a trust is met. This single element alone is not enough to create a trust for Medicaid purposes, but it is a crucial one that should be avoided. Because the gifts, in this context, always originate from the nursing home resident, and the gifts are not made pursuant to a will, any mechanism to hold the funds on the nursing home resident's behalf made pursuant to his direction could meet several of the indicia of a post 1993 self-settled trust. This risks a

finding the funds are available for nursing home costs and that the nursing home resident is ineligible to receive Medicaid.

D. *Use of Non-Probate Ownership Forms*

Use of joint and survivor or transfer on death accounts amongst the children who receive the gifts is a technique that many families use. They may do so to set aside an amount equivalent to some or all of the strategic reserve. These ownership forms concentrate assets and make it more likely they may be available for years. If there is any agreement or understanding, based on directions given by the nursing home resident, that the funds are the strategic reserve, then there is a risk this could be deemed a "legal instrument or device similar to a trust," and Medicaid eligibility could be denied. In spite of this risk, many families still proceed with this type of ownership structure.

The importance of not accepting or taking direction from the nursing home resident should not be overlooked or downplayed. If a trust benefits the nursing home resident, then it must be disclosed in the Medicaid application. Whoever applies for Medicaid benefits must acknowledge the answers given are true. Violating this oath could lead to a criminal prosecution, imprisonment, and a denial of Medicaid benefits.

A competing consideration is the desire to use the gifts as a mandatory, enforceable strategic reserve. To stay legal, there cannot be a wink and a shrug agreement that the gifts are not controlled by a trust when, in fact, this is exactly what is intended. Understanding how these rules function is acceptable and necessary in order to make a plan work successfully. The nursing home resident who makes the gifts, and the family participating in the process, must play by the rules. Taking steps to preserve sufficient funds to constitute a strategic reserve is not the same thing as establishing a trust to

benefit the donor, but it could be construed as such an attempt. An intent, which originates from the nursing home resident, to hold a specific set of assets to benefit the nursing home resident is a key element in establishing a trust. The parent cannot give the assets subject to instructions to form a trust to benefit him, nor can the family, at his direction, use those funds to form such a trust. The only protection the parent making the gifts can have, if he does not have LTHC, is the hope that his children would not let him down if he needs their help.

If the children receiving the gifts wish to hold a strategic reserve, then keeping the resources together has some risk of appearing to be part of a trust arrangement. However, there are advantages to doing so. The more accounts holding gifts, the greater the risks that the funds will be dissipated. Each of the risks attendant in these circumstances increases with the number of accounts and with the number of owners. By going from one owner to two, or from one account to two, the risks are doubled. Due to this logic, it makes sense to try to keep the gifts in the fewest number of hands, and accounts, as possible.

The risk that Medicaid would deem these funds available for the parent's use and deny benefits is one with which many families are comfortable. If application for Medicaid does not occur until after the look back period has passed, then the caseworker would have no reason to ask about transfers made prior to this time. This makes it unlikely the accounts would ever come to Medicaid's attention. If there is a trust that benefits the nursing home resident, it must be disclosed. But, if there is no agreement or understanding to use the proceeds for the parent based on "the direction of or upon the request of the nursing home resident," then there can be no "trust." Just having enough

funds in these accounts sufficient to comprise part of, or all, of a strategic reserve does not necessarily mean they are held for this purpose at the parent's direction or that they would be used in this fashion.

Some may argue that if the children receive the gifts, then this money becomes their own. If they then use their own assets to set up the non-probate accounts, then the funds did not come from the nursing home resident. Accordingly, there is no trust to benefit the nursing home resident even if the donor gave instructions or directions to follow this course. I do not advise such a strategy. I believe the wiser course is for there to be no instructions or directions from the nursing home resident regarding these matters. To stay on the right side of the law, he should make unconditional gifts … period.

There are legitimate reasons, other than using it as the strategic reserve, for choosing the non-probate ownership format. One of the family members may have investment expertise from which all of them could benefit. Owning it in this manner would promote this goal. Investment clubs all over the country are formed in a similar fashion and for the same purpose. Further, keeping the funds together, and knowing one's brothers and sisters are monitoring the accounts, promotes savings and provides an incentive to avoid spendthrift ways.

Use of joint and survivor accounts can promote a concentration of assets. Normally, up to three owners can be named on joint and survivor accounts. If any of the gift recipients dies, then the funds would remain in the same account and continue to be owned by the donor's children. Use of this non-probate format keeps the assets away from the deceased child's spouse, children, and creditors. It also permits the other

siblings to monitor the assets and decrease the odds that a lone owner would make unauthorized withdrawals of the funds. At the parent's death, each of the children could withdraw equal amounts and avoid making gifts to each other.

Placing all of the gifts in the name of one child, and having that child, in turn, list his siblings as beneficiaries of a transfer on death account, is a similar mechanism. Although multiple statements could be sent to all of the children and promote a common monitoring of the proceeds, if the children intend to equally share the proceeds when the parent dies, then difficulties can arise at that point. If the owner refuses to share the proceeds with his siblings, then they may not have a legal right to take their share. Further, if significant amounts are involved, then if the sole owner gives these funds to his brothers and sisters, then it may trigger the requirement to file a gift tax return.[37]

A weakness with the joint and survivor or transfer on death account is that only one Social Security Number may be used. This causes a reporting of all of the income to one person. If significant amounts are involved, then this could be unfair to the recipient. The children could rotate numbers, or make a distribution to pay the resulting taxes, but this could get burdensome. Use of a limited liability company could resolve this issue in a less cumbersome manner.

E. *Limited Liability Companies*

A more sophisticated approach to concentrating the gifts is to use a limited liability company (LLC). Keep in mind that all of the risks of the LLC being considered a trust to benefit the nursing home resident, as discussed with the procedures for using non-probate accounts, are applicable.

[37] I discuss gift tax considerations in this article at Page 46.

Once the children receive the gifts from the parent, they would then establish an LLC in which each of them owns a membership. They would then place the funds into an account owned by the LLC or transfer the real estate into the LLC's name. The LLC would have its own tax identification number. This would enable the interest and dividends, as well as deductions and other tax events, to be reported to the children each year on a K-1, which is a reporting document similar to a 1098 or 1099. This would get around the problem with joint and survivor or transfer on death accounts that require use of one Social Security Number, thereby causing one child to receive all of the tax consequences.

The LLC could also provide more options in the event one of the children predeceases the parent. In the joint and survivor or transfer on death model, the grandchildren or surviving spouse would not inherit the decedent's share. However, the Operating Agreement of the LLC, in the case of real estate, could call on the surviving children to buy out their deceased sibling's share, thereby making the proceeds available to the surviving issue and spouse. Or, the Operating Agreement could provide that the LLC would be liquidated, and all of the proceeds paid to its members, upon the death of the parent.

The downside to use of an LLC is its expense and sophistication. An attorney must draft the Operating Agreement. Tax returns must be prepared and filed each year for the company. Nevertheless, an LLC can serve as a more flexible vehicle for concentrating the gifts and controlling their dissipation than joint and survivor or transfer on death arrangements.

F. *Life Estates/Life Leases*

A life estate or a lifetime lease is an arrangement with real estate that can permit a parent to make a gift of their residence to their children, yet preserve their right to live there.

A life estate grants a right to live in and use realty for life. At the tenant's death, the real property passes to the beneficiaries specified in the instrument that created it. As a non-probate form of ownership, at death it is not necessary for probate proceedings to pass along title to the new owners. Although this feature makes the State's right of recoupment more difficult, it has other elements that make it attractive in this context.

If the Community Spouse resides in the home, then the residence subject to a life estate remains an exempt resource.[38] If the unmarried nursing home resident owns the life estate, then it is assigned a value that would likely be a fraction of the actual fair market value.[39] The children could purchase it for this reduced amount if necessary. Moreover, if the parent dies owning a life estate, then the children would receive a step-up in basis to its fair market value at the parent's death.

A similar arrangement may be accomplished through a lease. In this scenario, the parent gives or sells the real estate to the children, then the children or their LLC enter into a lease with the parent. The terms typically involve the right to live there for the rest of the parent's life in exchange for the parent paying rent, which should be in an amount no less than the insurance, taxes, and normal maintenance costs. The lease would also terminate after a few months of vacancy. By recording the lease or a memorandum of it,

[38] OAC §5101:1-39-32 (D)(1)(b) and (D)(2)(b).
[39] As an example, for a 65 year old person owning a life estate, if the property is not mortgaged, then the life estate is worth 30.033% of the County Auditor's appraised value for Medicaid purposes. See OAC §5101:1-39-32(F), CFR §20.2031-7, and IRS Publication 1457.

this would protect the parent's right to live there in the event the child or the LLC encounters problems with creditors.

As the reader may expect, there are several disadvantages to using life estates and life leases. Granting a life estate is a gift. Doing this within the look back period creates all of the same issues as any other type of bequest. The Medicaid rules have formulas for valuing the life estate. If the gift is large enough, then it may trigger a duty to file a gift tax return. Further, it could trigger the duty to file an Ohio estate tax return and pay the taxes.[40] Moreover, use of a life estate or life lease may make it difficult, if not impossible, to mortgage or sell the premises while the parent is alive. Further, the IRS imposes some limitations on the ability to recognize losses, or capital gains instead of regular income, when related persons are parties to the same transaction, so consultation with a tax advisor would be advisable before a child depreciates the property, recognizes losses, or pays capital gains on a subsequent sale.[41]

G. *Loss of Basis Step-Up*

As discussed at Pages 17 to 18, a disadvantage to making gifts is a loss of the opportunity for the children to receive a step-up in basis of assets they would have inherited from a parent. Although making gifts can, in some circumstances, save assets from potential nursing home expenses, the children who receive the assets may also realize a very low basis in these items. If the children inherit the assets, then they would receive a step-up in basis to the fair market value of the item at the parent's death. This can result in a significant savings of capital gains taxes when the item is sold. Of course,

[40] If all gifts, other than to the decedent's spouse, within three years of death exceed $338,333, then there is a duty to file an Ohio estate tax return and pay the taxes. A life estate could count as such a gift. See ORC §§5731.05, 5731.06, and 5731.21.

one can also argue that if the assets are not given away, then liquidating and spending the proceeds on costs that Medicaid could have paid is a form of 100% taxation.

H. *Gift and Estate Tax Consequences*

Whenever a person gives more than $12,000 in a year to an individual, then he must file a gift tax return.[42] In nearly all cases, the return is due on or before the normal April 15 deadline of the year after the event took place.

In this context, it would be extremely rare for a gift tax to be payable. This is because the donor may give away during his lifetime up to one million dollars.[43] If the parent in these circumstances made significant gifts during his lifetime, then hopefully he is still wealthy. If so, then it is unlikely he would need to be concerned about preserving his right to receive Medicaid.

An advantage of filing a gift tax return is that it can serve as a means of verifying, to a caseworker, that gifts were made on a certain date and in a certain amount. The disadvantage is that sometimes the information needed to prepare the gift tax return is difficult or time consuming to obtain. One must list the donor's basis in the property. Many times the documents necessary to prove the donor's basis are not immediately available. It can prove time intensive to locate them, and sometimes it is not possible at all. Once the preparer of the return has the information, and he has the fair market value of the item as of the date of the gift, preparation of the return is not too difficult and should not be expensive.

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[41] See, generally, 2007 US Master Tax Guide at Paragraph 1717 (Pages 552-553), Paragraph 1788 (Pages 572-573), and Paragraph 1835 (Page 580).
[42] Paragraph 2911, Page 791, 2007 US Master Tax Guide; 26 USC §6019.
[43] Actually, one may give away more than $1 Million in a lifetime because gifts in the exclusion amount of $12,000 or less do not count against the $1 Million limit. Paragraph 2910, Page 791, 2007 US Master Tax Guide; 26 USC §2505(a)(1).

Except for bequests to a surviving spouse, Ohio imposes an estate tax upon estates exceeding $338,333. Ohio includes, for purposes of ascertaining the taxable estate, all gifts made within three years of death.[44] It also includes all property subject to a life estate whether or not it is transferable. Therefore, gifts in these circumstances may leave the family responsible for filing and paying Ohio estate taxes even though there are no assets transferred at death. Keep in mind, though, that the estate tax would have been payable if the nursing home resident died owning the assets. Further, the peak Ohio estate tax rate is 7% for amounts exceeding $500,000.[45] As stated before, payment of nursing home costs could be interpreted as a 100% tax, so in comparison the estate taxes may not be so onerous.

VIII. Contacting the Author

I hope that you find this article informative and understandable. If you have questions, then you may contact me at glovett@lovettlawoffice.com or (937) 667-8805. There's never a charge for the first few minutes whether by phone or email.

[44] See the discussion at Page 45.
[45] ORC §5731.02.