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The Need for Planning

One of the greatest fears of older Americans is that they may end up in a nursing home. This not only means a great loss of personal autonomy, but also a tremendous financial price. Depending on location and level of care, nursing homes cost between $50,000 and $150,000 a year.

Most people end up paying for nursing home care out of their savings until they run out. Then they can qualify for Medicaid to pick up the cost. The advantages of paying privately are that you are more likely to gain entrance to a better quality facility and doing so eliminates or postpones dealing with your state's welfare bureaucracy--an often demeaning and time-consuming process. The disadvantage is that it's expensive.

Careful planning, whether in advance or in response to an unanticipated need for care, can help protect your estate, whether for your spouse or for your children. This can be done by purchasing long-term care insurance or by making sure you receive the benefits to which you are entitled under the Medicare and Medicaid programs. Veterans may also seek benefits from the Veterans Administration.

Medicare

Medicare Part A covers up to 100 days of "skilled nursing" care per spell of illness. However, the definition of "skilled nursing" and the other conditions for obtaining this coverage are quite stringent, meaning that few nursing home residents receive the full 100 days of coverage. As a result, Medicare pays for only about 9 percent of nursing home care in the United States.

Medicaid

For all practical purposes, in the United States the only "insurance" plan for long-term institutional care is Medicaid. Lacking access to alternatives such as paying privately or being covered by a long-term care insurance policy, most people pay out of their own pockets for long-term care until they become eligible for Medicaid. Although their names are confusingly alike, Medicaid and Medicare are quite different programs. For one thing, all retirees who receive Social Security benefits also receive Medicare as their health insurance. Medicare is an "entitlement" program. Medicaid, on the other hand, is a form of welfare -- or at least that's how it began.

Also, unlike Medicare, which is totally federal, Medicaid is a joint federal-state program. Each state operates its own Medicaid system, but this system must conform to federal guidelines in order for the state to receive federal money, which pays for about half the state's Medicaid costs. (The state picks up the rest of the tab.)

This complicates matters, since the Medicaid eligibility rules are somewhat different from state to state, and they keep changing. Both the federal government and most state governments seem to be continually tinkering with the eligibility requirements and restrictions. This has most recently occurred with the passage of the Deficit Reduction Act of 2005 (the DRA) which significantly changed rules governing the treatment of asset transfers and homes of nursing home residents.

Transfers

Congress has established a period of ineligibility for Medicaid for those who transfer assets. The so-called "look back" period for all current transfers is 60 months.

Trusts

The problem with transferring assets is that you have given them away. You no longer control them, and even a trusted child or other relative may lose them. A safer approach is to put them in an irrevocable trust. A trust is a legal entity under which one person -- the "trustee" -- holds legal title to property for the benefit of others -- the "beneficiaries." The trustee must follow the rules provided in the trust instrument. Whether trust assets are counted against Medicaid's resource limits depends on the terms of the trust and who created it.

A "revocable" trust is one that may be changed or rescinded by the person who created it. Medicaid considers the principal of such trusts (that is, the funds that make up the trust) to be assets that are countable in determining Medicaid eligibility. Thus, revocable trusts are of no use in Medicaid planning.

Income-only Trusts

An "irrevocable" trust, on the other hand, is one that cannot be changed after it has been created. In most cases, this type of trust is drafted so that the income is payable to you (the person establishing the trust, called the "grantor") for life, and the principal cannot be applied to benefit you or your spouse. At your death the principal is paid to your heirs. This way, the funds in the trust are protected and you can use the income for your living expenses. For Medicaid purposes, the principal in such trusts is not counted as a resource, provided the trustee cannot pay it to you or your spouse for either of your benefits. However, if you do move to a nursing home, the trust income will have to go to the nursing home.

You may also choose to place property in a trust from which even payments of income to you or your spouse cannot be made. Instead, the trust may be set up for the benefit of your children, or others. These beneficiaries may, at their discretion, return the favor by using the property for your benefit if necessary. However, there is no legal requirement that they do so.

One advantage of these trusts is that if they contain property that has increased in value, such as real estate or stock, you (the grantor) can retain a "special testamentary power of appointment" so that the beneficiaries receive the property with a step-up in basis at your death. This will also prevent the need to file a gift tax return upon the funding of the trust.

Remember, funding an irrevocable trust can cause you to be ineligible for Medicaid for the following five years.

Protection of the House

After a Medicaid recipient dies, the state must attempt to recoup from his or her estate whatever benefits it paid for the recipient's care.

Life Estates

For some people, setting up a "life estate" is the most simple and appropriate alternative for protecting the home from estate recovery. A life estate is a form of joint ownership of property between two or more people. They each have an ownership interest in the property, but for different periods of time. The person holding the life estate possesses the property currently and for the rest of his or her life. The other owner has a current ownership interest but cannot take possession until the end of the life estate, which occurs at the death of the life estate holder. As with a transfer to a trust, the deed into a life estate can trigger a Medicaid ineligibility period of up to five years.

Life estates are created simply by executing a deed conveying the remainder interest to another while retaining a life interest.

Trusts

Another method of protecting the home from estate recovery is to transfer it to an irrevocable trust. Trusts provide more flexibility than life estates but are somewhat more complicated. Once the house is in the irrevocable trust, it cannot be taken out again. Although it can be sold, the proceeds must remain in the trust. This can protect more of the value of the house if it is sold. Further, if properly drafted, the later sale of the home while in this trust might allow the creator of the trust, if he or she had met the residency requirements, to exclude up to $250,000 in taxable gain, an exclusion that would not be available if the owner had transferred the home outside of trust to a non-resident child or other third party before sale.

Those who are not in immediate need of long-term care, may have the luxury of distributing or protecting their assets in advance. This way, when they do need long-term care, they will quickly qualify for Medicaid benefits. Giving general rules for so-called "Medicaid planning" is difficult because every client's case is different. Some have more savings or income than others. Some are married, others are single. Some have family support, others do not. Some own their own homes, some rent. Still, the preceding techniques are common strategies and tools that are typically used in Medicaid planning. To be certain of your rights, call me for a free consultation and I can guide you through the complicated rules of the different programs and help you plan ahead.