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Estate, Trust, Tax and Long Term Care Planning

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SPECIAL REPORT

- Community Spouse Planning Considerations and Techniques -

Applying for Medicaid for a spouse can be emotionally difficult, but add the application and eligibility criteria on top and the whole process can be daunting. Community Spouses hear stories of houses being taken and having to spend down all their assets to qualify their spouse for Medicaid. The alternative to Medicaid is not overly enticing either, as the cost of care for facilities keeps rising. For 2020, the average cost of skilled care in Colorado is $8,758 per month. For most people this cost alone would decimate a couple's savings in no time. Add the community spouse's living expenses on top of that and couples sometimes spend $8,000 - $10,000 a month just to live minimally. Rightfully so, we see many community spouses in a manic state trying to decide how to adequately care for their spouse and still be able to pay for their own living expenses.

The good news is that Medicaid regulations carve out protections for Community Spouses. The Department understands Community Spouses need to afford to continue to live in the community and sustain expenses unrelated to the Institutionalized Spouses. The three main protections afforded Community Spouses are the following:

1. Community Spouses can keep $128,640 of additional assets above the exempt resources.
2. Community Spouses are allocated a portion of the Institutionalized Spouses income depending on certain factors.
3. The Department gives separate treatment to resources post-eligibility.

These three protections allow Community Spouses to have a nest egg of money they can use for their own expenses and their long term care in the future. Additionally, in some circumstances income can be diverted to the Community Spouse from the Institutionalized Spouse. This increases the monthly income for the Community Spouse to assist with paying bills. Finally, once the institutionalized individual has been approved for Medicaid, there is a separate treatment of resources between spouses. This allows the Community Spouse to plan for his or her own long term care planning.

To best explain the planning considerations and techniques, let's look at John and Mary, our imaginary couple. John is 85, recently suffered a stroke and will need skilled care for the remainder of his life. Mary is 83, lives at home and is in relatively good health. Their resources include a house owned free and clear worth approximately $400,000, investments worth $100,000, checking and savings accounts worth $50,000 and two vehicles (one worth $5,000 and the other worth $10,000). John's gross monthly income is $4,500 and Mary's is $1,000. In order for John to qualify for Medicaid, he and Mary will need to spend down approximately $25,000.

So keeping John and Mary in mind, here are the techniques and planning considerations they need to consider.

<u>Income techniques and planning considerations.</u>

- **Paying down debt**

  If we change the facts of John and Mary's financial situation slightly and add credit card debt of $10,000 and an encumbrance on the $10,000 vehicle of $8,000, you can see how this approach works. This technique can be used for all kinds of debt but some debt is more advantageous to eliminate than others. We will discuss this more later. The monthly payments on credit card debt and car loan can be daunting along with all the other house bills if John's income is not available to assist with those bills. Paying down debt so there are no monthly payments can ease the monthly financial burden on Mary. Using $18,000 of the $25,000 is a good way to spend down the assets so Mary does not have monthly payments.

Again, this strategy likely will need to be implemented along with another strategy to complete the spend-down.

- **Purchasing a Medicaid compliant annuity**

The Community Spouse has the ability to purchase an annuity to increase income. Medicaid compliant annuities are used as a spend-down technique to turn a lump sum of money into an income stream for the Community Spouse. In our example, Mary may require $3,500 a month to pay for her living expenses. Under the spousal income rules, she would only be entitled to a minimum of $2,114 or a maximum of $3,216 after income shifting from John's income. Even at the maximum, her income would fall short of her monthly needs. In circumstances like these, it may be in Mary's best interest to purchase an income stream as the spend-down technique. This would allow Mary to receive $2,500 a month for 10 months if the entire $25,000 is used to purchase the annuity.

This type of planning should be done with much consideration because there are certain restrictions with using these types of annuities. Beneficiary designations must comply with the Medicaid Regulations in order to effectuate the purchase without causing a transfer penalty. This type of planning is especially important if the Institutionalized Spouse is not likely to live very long and there are no survivor benefits associated with the Spouse's income. Protecting the Community Spouse in this way is extremely important.

- **Increase expenses**

The amount of the Institutionalized Spouse's income which will be transferred to the Community Spouse is dependent on the expenses of the Community Spouse. In some circumstances, it makes sense to increase the Community Spouse's expenses so more income is allocated to the Community Spouse. In our example, if Mary and John's resources were $50,000 and they owned their house free and clear, it may be a good idea to take out a mortgage on their house of $30,000. If they did so, their resources would be $80,000 and they would have a monthly mortgage expense. Mary would be allocated additional income from John each month to pay the mortgage. The effect of this type of planning would be to free up additional cash for Mary if she needs it, while also paying for the mortgage with John's income, which Mary otherwise would not have received. This can work nicely in certain circumstances.

Resource techniques and planning considerations.

- **Upgrading a residence or vehicle**

One planning tool Mary has is to use the $25,000 which needs to be spent down on making upgrades or modifications to her home. Keeping her own long term needs in mind, she may want to install grab aides and/or ramps or remodel her bathroom or bedroom to anticipate her future needs. Improving the house so Mary can stay at home as long as possible is good forethought and planning. Additionally, Mary may want to sell both cars and purchase a newer vehicle which will provide her safe, comfortable transportation as she ages.

- **Prepaying for funeral and burial plans**

Converting non-exempt assets to exempt assets has long been a valuable way to spend down assets to qualify for Medicaid. With the $25,000 Mary and John need to spend down, they can purchase funeral and burial plans. Unless they intend to have exceptionally extravagant funerals, they will likely not spend the entire $25,000 on prepaid funeral plans so additional spend-down techniques will need to be employed. This strategy allows John and Mary to be able to use the spend-down money on something which will retain value. One concern many of our clients share is not burdening their children financially after their death with funeral costs. This is an excellent way to pass value on to their children.

Estate Planning techniques and planning considerations.

- **Transfer assets to Community Spouse**

During the application process and within a year from the determination of eligibility for the Institutionalized Spouse, all of the assets should be transferred into the Community Spouse's name. This is important to make sure the Institutionalized Spouse is not over-resourced at their redetermination. It is important also because if the Community Spouse dies, any assets held jointly between the spouses will be transferred back to the Institutionalized Spouse, which could be problematic.

- **Updating estate planning to protect the institutionalized spouse**

One of the most important things a Community Spouse needs to do is to update his or her estate planning. A typical estate plan for a married couple is what we call "I Love You" wills where the spouses leave everything to each other. This type of planning is counterproductive once one spouse is on Medicaid. If the Community Spouse dies with an "I Love You" will, then all the assets in the Community Spouse's name will be transferred to the Institutionalized

Spouse, causing the Institutionalized Spouse to lose Medicaid benefits. It is important to update the Community Spouse's estate plan to protect the Institutionalized Spouse as much as possible.

It is also important to know a Community Spouse cannot disinherit the Institutionalized Spouse. Colorado has statutory law which does not allow for one spouse to disinherit completely the other spouse. This is called a spousal election. The law allows for a disinherited spouse to elect against the other spouse's estate plan and take some of the assets, depending on the asset's allocation. In the Medicaid regulations, if Mary tries to disinherit John, the regulations will require John to make an election against Mary's estate. This election right needs to be considered when preparing estate planning for the Community Spouse.

- **Make transfers after institutionalized spouse is on Medicaid**

The regulations state after an Institutionalized Spouse has been determined eligible for Medicaid, the Community Spouse's assets are no longer considered for redetermination purposes. This allows a Community Spouse to employ long-term care strategies which may include making transfers of assets which do not impair the Institutionalized Spouse's benefits. In our example, Mary may want to make a transfer to implement an asset protection long-term care plan. She will need to wait until John has been determined eligible for Medicaid and then she can make the transfer.

- **Using a Personal Service Contract to stay at home**

In some circumstances Community Spouses discover living alone is more difficult than they anticipated. To facilitate the Community Spouse staying at home as long as possible, we often use Caregiver Agreements (also known as Personal Service Contracts) in which the Community Spouse hires a family member or friend to provide services for them at home. This allows for a transfer of assets between the Community Spouse and children or other relatives. In our case, if Mary needs assistance with personal care or financial management, she can enter into an agreement with her daughter to provide care. The agreement spells out exactly the services to be provided and compensation to be paid. Keep in mind, this is income to the child and must be reported. It is imperative under the rules the agreement be in writing and notarized, prior to any services being commenced or Medicaid may treat any payments as a gift which could be problematic if the community spouse needs Medicaid benefits in the future.