THE MEDICAID CRISIS PLAN

by

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The Deficit Reduction Act of 2005 greatly limited the types of planning available to families facing a crisis of health care. Practitioners across the state are visited on a weekly, or perhaps daily, basis by families who have received the news that around the clock care is necessary for a parent or loved one. A frequent question that almost inevitably follows is, "Isn't there anything we can do to protect any assets?"

Crisis Planning for Chronic Care (Nursing Home) Medicaid

When a family approaches and asks for guidance on setting aside some of the family's wealth to pass along to heirs when nursing home admission is imminent, the plan is, most often, the Promissory Note/Gift plan. You will recall that the Deficit Reduction Act (DRA)[1] changed the timing at which a penalty period for gifts begins to run. Prior to the DRA, the penalty period for any transfers began to run on the first day of the month following the month of transfer. In this way, a transfer could be made, the penalty period calculated, and then the family could "wait out" the running of the penalty period. At the end of the penalty period, the transfer was no longer a consideration in Medicaid eligibility.

The DRA changed that. The penalty period begins to run on the LATER of:

(1) the date when

(a) the Medicaid applicant:

(i) is resource eligible;

(ii) is income eligible;

(iii) requires nursing home level care; and

[1] See 06 ADM-05.

(iv) has filed a Medicaid application; **and**

(b) no other ineligibility period is outstanding; **or**

(2) the first day of the month after which assets have been transferred.[2]

Therefore, the applicant must be in a nursing home, have no more than $14,550 in his/ her name, and have a Medicaid application submitted in order for the penalty period to begin running. It is the careful coordination of these factors that the experienced elder law attorney must undertake in order to have a successful Promissory Note/Gift Plan.

The premise of the Promissory Note/Gift Plan is the depletion of the applicant's assets in a simultaneous gift and loan transaction. A portion of the applicant's assets are gifted away, and, at the same time, the remainder of the applicant's excess resources is loaned away in a DRA compliant Promissory Note.[3] In one fell swoop, the applicant is now below the $14,550 resource level. The penalty period for the transfer can begin, provided the applicant is receiving nursing home care and a Medicaid application is submitted. During the running of the penalty period, the loaned funds are returned to the applicant on a monthly basis, thereby providing the applicant with additional funds with which to privately pay the nursing home until such time as the penalty period expires.

The Promissory Note/Gift Plan was the logical planning tool that remained after the implementation of the DRA. As this type of planning began to develop in 2006, its implementation was, of course, met with resistance from the Local Department of Social Services (LCDSS). Some fair hearing decisions set the tone, allowing properly implemented Promissory Note/Gift plan to proceeds.[4] With solid legal footing underneath, practitioners must now begin the tedious but valuable journey into Promissory Note/Gift planning.

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[2]See GIS 06 MA/016.

[3] See GIS 06 MA/016.

[4] See Matter of Geraldine A., Fair Hearing #4733466Z, Albany County, decided August 29, 2007.; Matter of Anna M., Fair Hearing # 4733471N, Albany County, decided August 29, 2007; Matter of Mary K, Fair Hearing #4733465H, Albany County, decided August 29, 2007.

Beginning the Promissory Note/Gift Plan

The gathering of information is critical. Rough numbers can be used to illustrate to the client the broad strokes of how the plan will work, but precise figures are needed before a plan can be finalized. How your practice decides to gather the information is a personal decision. Some firms do not start calculations until all documents are in; some firms ask for current statements of holdings and then rough out numbers. Other firms, like me, have different team members working on different portions of the plan throughout the month.

1. Determine the Medicare Cut Off Date. The Promissory Note/Gift Plan will only work when the applicant financially qualifies for Medicaid health benefits. This means the applicant must be receiving nursing home care, is “income eligible” and has assets below the permissible threshold. Because New York is an income spend-down state, Medicaid will only provide coverage when the applicant’s medical needs exceed his or her ability to pay. Therefore, in order to be “income qualified” for Medicaid benefits, the applicant must have medical bills that exceed his or her income. If Medicare is paying for the applicant’s rehabilitative care in the nursing home, chances are that the applicant will have supplemental insurance to cover the co-pay, or will have enough income to pay the co-pay for the care. As a result, he or she will not have medical expenses that exceed income, so, the applicant will not be income eligible. Therefore, determining the precise day on which Medicare will no longer be paying for the care in the nursing home is critical to the timing of the Promissory Note. Unfortunately, this may be mid-month or, even worse, with only a day or two left in the month. Timing is everything!

2. Assess the Assets. It is critical to know what the applicant has. Remember which assets must be counted…***everything that is not exempt***! Ask about life insurance cash values; ask about nursing home deposits; ask about those pesky stock shares that were issued when life insurance companies went public years ago; ask about those 529 plans that the applicant set up for her grandkids; ask about the joint bank account the applicant holds with her sister…all of these things will either need

to be factored into the Promissory Note/Gift Plan, or fully explained and documented to LCDSS if they are not to be considered assets of the applicant.

3. Assess the Prior Transactions. Put on your LCDSS Caseworker hat. You must review every financial record that you will be submitting to LCDSS.[5] If there is a transaction the applicant can't explain, it will be considered a gift. You must know what things are going to be considered prior transfers/old gifts in order to arrive at an accurate Promissory Note/Gift Plan.

4. Assess the Income. You must examine the income of the applicant in minute detail. You need to know the gross income from all sources – Social Security or Railroad Retirement Benefits; pensions; required minimum distributions from IRAs; rental income from a life estate or any other property; VA benefits; long term care insurance benefits; disability insurance benefits; income from trusts of which the applicant is a beneficiary; and dividend and income from investments. Do not be caught unprepared! Compare 1099s and award letter from Social Security and pension administrators. Do not trust bank statement or the fact that you see the same deposit every month going into an account. Some pensions pay a 13th check at some point during the year. Look, look, and look again! You must then know the exact value of the only the permissible offset– health insurance expenses. In addition, review pension statements carefully to see if the pension administrator reimburses the applicant for Medicare premiums. If so, this must be taken into account. Determine if Medicare premiums are withheld from income. Determine if health insurance premiums are withheld from pensions. Determine if the applicant pays a monthly or quarterly premium for health insurance. Determine if the applicant has been having income taxes withheld from income. All of these factors must be addressed in order to arrive at an accurate Promissory Note/Gift Plan.

5. Assess the TRUE cost of care. You must know, precisely, the exact cost of

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[5] While the Medicaid application itself suggests that LCDSS review all transactions of $2,000 or more, that figure is merely *suggestive*; individual LCDSS are permitted to review transactions of whatever amount they wish, and your author has experienced upstate counties reviewing transactions (deposits and withdrawals) of $500.

daily care, plus the then-prevailing NYS nursing home assessment (currently 6.8%).[6] It will also benefit you to know what portion of the nursing home assessment is refundable to your client as well.

6. Assess the Outstanding Liabilities. You must determine if the applicant has debts that must be paid before you calculate your Promissory Note/Gift Plan. Debts can include paying your fee and prepaying for funeral costs. Remember, we are trying to arrive at excess resources, so the total of all gross resources, minus expenses that will be paid in the immediate future, result in the excess resource figure from which we will begin our plan. Outstanding medical expenses can be used to offset excess assets if needed.

7. Gauge Your Client's Need for Retained Assets. There can be great flexibility in the Promissory Note/Gift Plan if the client is not wed to the concept of having $14,550 in his/her name on the first day of the month in which the plan begins. Because there will inevitably be a surprise – interest that posts; a forgotten check that didn't clear in time; a long lost life insurance policy – it is my practice to prepare the applicant and the family for the fact that my plan will not permit him/her to retain the full $14,550. I do, however, carefully demonstrate to the applicant and the family that the retained funds will be sufficient and that costs will be covered from a variety of other avenues.

8. Assess the Liquidity of Assets. Some of your decisions may be made for you if it turns out that the applicant has significant illiquid assets that cannot easily be converted to cash. Depending on the timing of the plan, and depending upon the income tax and capital gains basis of various assets, you may be forced to permit your applicant to retain life insurance policies with cash values as his/her retained funds. (After eligibility, liquidation can occur.) Another example might be the gifting of a remainder interest in a home with a retained life estate, so as to preserve step up in basis benefits upon death of the applicant, using liquid resources for the loan. There is a horrible feeling when you arrive at a plan based on the presumption that the

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[6] See Public Health Law § 2807-d(2)(b); Tax Law, Article 22, Section 606(hh) permits the refund of a portion of this assessment; see also NYS Dept. of Taxation Form IT-258, Claim for Nursing Home Assessment.

assets are all easily transferrable, only to find out that you're over-resourced and can't do anything about it!

9. Remember Your Penalty Period Divisor. The penalty period will be calculated based upon the regional rate of nursing home care as prescribed by New York State for the region in which the facility is located. So, it is possible to have a Nassau County resident applying for Medicaid to pay for coverage of her stay in an Albany County nursing home. The regional rate when calculating the penalty period in 2014 will be $9,212 based upon the northeastern regional rate and not $12,112 based upon the Long Island regional rate.[7]

10. Put Your Numbers to Work. A good first step is to determine what it is that your Promissory Note must generate for your applicant to permit him/her to meet the cost of care. Be aware that there is a requirement that the applicant's monthly income cannot exceed the cost of care in order for that applicant to be considered eligible for Medicaid benefits. Therefore, if your applicant's regular net income and Promissory Note payment total an amount that exceeds the monthly cost of care, your plan will not work.

How to Do the Math

There are software programs that exist that can generate a Promissory Note calculation for you. Other people do the math with a pencil and paper. Still others have developed an Excel spreadsheet or other database-like program to determine how a promissory note might work. In reality, you need to have a good amortization calculator at your disposal because you must determine an actuarily sound promissory note (discussed below).

The Parties at the Promissory Note/Gift Party

Obviously, the well-versed elder law practitioner is the most important part of the Promissory Note/Gift Plan. However, a dependable, reliable paralegal is critical as well, as you will be reviewing voluminous documents – and perhaps in a very short

[7]See GIS 14 MA/003; see also 96 ADM-8, page 15.

period of time. In addition, you must have all the documents you need, and so the active participation of the applicant (or, most likely, the family) is also critical. Even if your letter of engagement and fee structure put the responsibility for securing all documentation on you and your firm, you will still need the applicant and family's input and guidance in explaining prior transfers and transaction that need additional documentation.

The discussion must then be had with the applicant as to who can be a suitable recipient of the gifted funds and who is a trustworthy borrower for the Promissory Note. Ideally, the Borrower will be someone with whom you, as the attorney, have a good working relationship.

Drafting the DRA Compliant Promissory Note

The actual Promissory Note document (which is a legal document to be prepared by qualified counsel only) must meet certain specifications in order to be acceptable to the local County Department of Social Services.[8] A Promissory Note meets the requirements of the federal DRA statue if it is (1) actuarially sound, as discussed below, (2) the monthly payment amounts are equal during the term of the note with no provisions for deferral or balloon payments at the end of the note, and (3) the promissory note is not cancelled (forgiven) upon your death. Failure to comply with these provisions is fatal to your plan.

A promissory note will be deemed actuarially sound if the payout period (the number of months the payments will be made under the note) is proportionately related to no more than a person's life expectancy. 06 AMD-05 provides that a Promissory Note is actuarily sound if it is calculated "in accordance with the actuarial publications of the office of the Chief Actuary of the Social Security Administration."[9] Using this life expectancy chart, our hypothetical 80 year old would have had a 7.31 year life expectancy if a male and a 8.95 year life expectancy if female. However,

[8]See 42 U.S.C.A. 1396p(c)(1)(I); see also 06 ADM-05.
[9] See 06 ADM-05, attachment VIII.

GIS 12 MA/025 was issued on October 1, 2012, providing an updated Life Expectancy Table. [10]Using the new life expectancy chart, that same 80 year old male has a life expectancy of 7.9 and a female has 9.43. This slight difference is, most like, irrelevant when discussing a Promissory Note plan because most Promissory Notes are in place for much less than 5 years. If an applicant had the funds to engage in a loan that would span more than 60 months, he/she wouldn't be doing a Promissory Note/Gift Plan and would instead simply transfer assets and wait until the expiration of the look back period.

While the DRA does not include this provision, it is advisable that the Promissory Note be non-negotiable. In other words, make the Promissory Note unable to be resold. A traditional Promissory Note can be sold between parties – much like your home's mortgage may have been sold to another bank. This negotiability gives the Promissory Note value and might result in other provisions of the Medicaid eligibility rules pulling the negotiable promissory note into the "available resource" category. Therefore, making your Promissory Note non-negotiable will be an added layer of protection.

The proper drafting the Promissory Note is critical, as an improperly drafted note can be deadly to the plan.[11] Geriatric care managers, Medicaid Advisors, and other non-attorney persons who attempt to undertake Promissory Note planning may very well wind up costing the applicant the precise assets he/she was attempting to preserve.

Doing the Math

With a well drafted Promissory Note document in hand, the question still remains…how much is the Gift, how much is the Note, and how will all of this work??

Different practitioners approach the plan differently. Some fix the amount of assets the applicant retains, and allow the Gift/Note numbers to be adjusted. Others prefer a gift number that doesn't include a partial month penalty period, allowing the

[10] See 12 MA/025.
[11] See Matter of Rose Pape, Fair Hearing #4732056R, February 15, 2007.

loan and retained assets figures to be adjusted. Others prefer to ensure the monthly loan repayment figure is as close to the actual cost of care (when added to other income) as possible.

Other factors to think about include building in a "cushion" in the applicant's retained funds and in the gifted monies in case the LCDSS caseworker identifies any transfers that you might have missed. You may also wish to consider whether the applicant will apply for and receive the refund on the nursing home assessment and/or an income tax refund. Both of these sums will assist in making the applicant and family more comfortable with the figures you present.

Finally, it is time to just put pen to paper and begin playing with the figures. A good starting rule of thumb is to try half the value of the excess resources. Plug that value in and calculate the penalty period, and then plug that number into the Promissory Note and see where the numbers come out. Remember to reserve some funds for the applicant! The manipulation of the figures can be a time consuming endeavor, even for those people using document drafting software or other calculators. However, the end results for the client can be tremendous, so take your time and good luck!

The Medicaid Crisis Plan

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Planning for Care at Home

- No look back period/no transfer penalty
- Coordinate planning for eventual nursing home needs
- Consider exempt transfers and/or purchases
- Determine whether waivered services are needed
- Use Pooled Trust for excess income/income spend down
- Choose your program carefully (NHTD v. MLTC)

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Planning for Care at Home (con't.)

- Consider consequences of planning for care at home on future chronic care/nursing home eligibility
  - While there is no look back period for home and community based Medicaid (and, as a result, no transfer penalty/penalty period), if chronic care Medicaid is needed within 5 years of any transfers made as part of the HCBM planning and application process, those transfers will impact eligibility for chronic care Medicaid

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No Homestead – Buying a Life Estate

- Deficit Reduction Act of 2005 stated that a purchase of a life estate by an A/R will be a transfer for less than full value (a gift) unless A/R resided in home for 1 year after purchase
- Even though value of life estate is disregarded when calculating value of assets of A/R, the life estate still does have a value
- 96 ADM 08, Attachment V provided the life estate valuation figures

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No Homestead – Buying a Life Estate (con't.)

- For example, 80 year old using this chart could acquire a life estate for 0.43659 of the value of the property
- However, radical change in 2011
- As part of the now-abandoned Expanded Estate Recovery, life estates were now to be valued using IRS Table S, which took into account the applicable federal midterm rate for the month of transfer

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No Homestead – Buying a Life Estate (con't.)

- 11 OHIP/ADM 8 provides that life estates are now to be valued by determining the IRC § 7520 rate, looking at Table S, and then applying the appropriate factor
- So, in September 2014, that same 80 year old could acquire a life estate for 0.16157 of the fair market value of the property
  - September 2014 had as its 7520 rate 2.2%

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No Homestead – Buying a Life Estate (con't.)

- Old way:
  - $500,000 home x 0.43659 = $218,295
- New way:
  - $500,000 home x 0.16157 = $80,785
- As a result, this is now a less attractive option for planning simply because the amount permitted to be transferred is significantly smaller
- But, it remains a mid-range planning tool

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The True "Crisis" Plan: Promissory Note/Gift Planning

- Because the Deficit Reduction Act of 2006 changed the date on which the Penalty Period for any transfer begins, the traditional "half-a-loaf" planning that was done pre-February 2006 is no longer possible
- "Half-a-loaf" had an applicant gifting away approximately ½ of his/her assets, immediately triggering the penalty period, retaining the balance to pay for care during the running of the penalty period
  - At the end of the penalty period, retained assets would have run out and Medicaid would start paying for care

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Promissory Notes (con't.)

- If traditional Half-A-Loaf is done, the applicant would spend down the retained half (arriving at the $14,550 of permissible retained assets for 2014), ***then*** the penalty period would run
- So, the post-DRA modification to the Half-A-Loaf plan is to gift away some, loan away the other

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Promissory Notes (con't.)

- Remember, penalty period runs on the LATER of the date when the A/R:
  1. is resource eligible;
  2. is income eligible;
  3. requires nursing home level of care;
  4. has filed a Medicaid application; and
  5. has no other ineligibility period outstanding

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Promissory Notes (con't.)

- A promissory note is "an unconditional promise, signed by the maker, to pay absolutely and in any event a certain sum of money either to, or to the order of, the bearer or designated person."
- To implement a gift-note plan, the attorney must draft a DRA compliant promissory note to evidence the loan made by the A/R, which will be repaid with interest over a specified period of time.

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Promissory Notes (con't.)

- DRA modified the rules governing the purchase of promissory notes, loans and mortgages. The DRA amends Social Security Act Section 1917(c)(1) by adding new rules governing the purchase of these investments (see Section 6016(c) of the DRA). New York adopted these rules (see 06 OMM/ADM-5)

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Promissory Notes – Critical Information Needed

1. Medicare Cut Off Date
2. Assets
3. Prior Transactions Review
4. Income
5. Cost of Care
6. Outstanding Liabilities
7. Need for Retained Assets
8. Liquidity of Assets
9. Penalty Period Divisor

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Promissory Notes – Critical Information Needed

- Medicare Cut Off Date: eligibility for Medicaid cannot occur until medical expenses exceed income; if A/R is having care at nursing home paid for through Medicare, then A/R does not have medical expenses that exceed income
- Prepare A/R and family for the uncertainty of this – when it happens on the 2d day of a 31 day month, a nursing home liability will accrue for the remainder of the month

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Promissory Notes – Critical Information Needed

- Assets: *Everything that is not exempt is counted*. Everything.
  - Security deposits at the nursing home
  - Life insurance cash values if owned by A/R
  - Stock (even the 16 shares someone owns as a result of life insurance companies going public years ago)
- Be prepared to prove exclusions/exceptions should apply (i.e., bank account held jointly with another is considered the A/R unless it can be proven A/R did not contribute)

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Promissory Notes – Critical Information Needed

- Review of Prior Transactions. Someone who gifted away $50,000 during the last 5 years is going to have a very different Promissory Note/Gift Plan than someone who has not made any gifts
- Be familiar with your LCDSS practices ($2,000 level of asset review? Review of deposits and withdrawals or just withdrawals?)

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Promissory Notes – Critical Information Needed

- Income. Get proof of income (don't take their word for it). Evaluate what is the gross income and what are the offsets
  - Income tax withholdings are not permitted – get them to stop
  - Health Insurance premiums are permissible, but identify true cost
  - Watch for 13th pension payments
  - Consider Long Term Care Insurance payments
  - RMDs and other distributions from retirement

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Promissory Notes – Critical Information Needed

- True Cost of Care. Prove it. Is the rate the A/R or family tells you the private room rate? The semi-private room rate? Does it matter? Does the price quoted include the 6.8% assessment or is that additional? Will additional medical expenses be incurred (*i.e.*, what health insurance does the A/R to have cover prescription costs)?

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Promissory Notes – Critical Information Needed

- Assess Outstanding Liabilities. Satisfying outstanding liabilities is permissible spend down if those liabilities belong to A/R. Include in your evaluation of "liabilities" permissible expenditures (home repairs, etc. if there is a Community Spouse), your legal fees and preneed funeral arrangements, if needed. Get those spent.
- Outstanding medical bills can be used to offset excess assets.

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Promissory Notes – Critical Information Needed

- Gauge A/R and Family's need for level of retained assets. Just because A/R is allowed to keep $14,550 doesn't mean the plan will work out that way.
  - In addition, prepare the family for the fact that the $14,550 (or a large part of it) may be illiquid resources that will then need to be liquidated.
  - Third Quarter plan may mean less assets needed (income tax refund and/or NH Assessment credit may mean influx of cash within 6 months)

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Promissory Notes – Critical Information Needed

- Assess Liquidity of Assets. Depending on how your pot of excess assets are comprised, your planning options may be limited.
  - How fast can you liquidate stock? Cash in life insurance or take a loan against it?
  - Can you annuitize an annuity? Is IRA in payout?
  - If your entire pot of excess resources are illiquid, does borrower (child) have sufficient cash to repay note?

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Promissory Notes – Critical Information Needed

- Remember Your Penalty Period Divisor. Just because it's a Suffolk County resident, doesn't mean we're using Suffolk County divisor.
  - GIS 14 MA/003 and 96 ADM 8, page 15 tells us that the regional rate for the region in which the facility is located will be used to calculate penalty period
- Therefore, if an application is going into Suffolk County based upon residency but for care in Albany, use $9,212 **and not** $12,112

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Get To Work!

- Draft your Note (partially)
- Calculate your Gift
- Calculate your Penalty
- Calculate your Loan
- Finalize your Note
- Direct A/R and Family on transfers
- Verify transfers
- Complete Medicaid Application
- Supervise repayment

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Drafting the DRA Compliant Promissory Note

- DRA rule: Funds used to purchase a promissory note, loan or mortgage are considered to be a transfer of assets unless all of the following criteria are met:
  - The repayment term is actuarially sound (see the actuarial standards offered by the Office of the Chief Actuary of the Social Security Administration);
  - The payments are made in equal amounts during the term of the loan, with no deferral of payments and no balloon payments; and
  - The promissory note, loan or mortgage prohibits the cancellation of the balance upon the death of the lender.

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Drafting the DRA Compliant Promissory Note (con't.)

- A promissory note complying with the DRA criteria will be considered a bona fide transaction, and the purchase of such an asset will not be classified as a transfer of assets.
- Given the clear language of the DRA, the drafting attorney will want to ensure that these criteria are met on the face of the note

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Drafting the DRA Compliant Promissory Note (con't.)

- Additional drafting tips:
  - Include language stating that the note is non-negotiable, non-assignable and otherwise non-transferable by the Promisee
  - This defeats the argument that the note could be considered a negotiable instrument (see Medicaid Reference Guide at page 296), and thus an available resource to the A/R, by means of potential resale of the investment to a third party.

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Drafting the DRA Compliant Promissory Note (con't.)

- Additional drafting tips:
  - Exclude otherwise standard note terms:
    - acceleration language in the event of default;
    - increase in interest rate upon default;
    - authorizing the collection of attorneys fees in the event of default;
    - other terms that would make the note attractive to a third party.
    - Include language expressly prohibiting pre-payment of the loan.

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Our Client

- On October 1, Daughter and Agent under Power of Attorney that you drafted a year ago comes in to talk about your client, Mom
- Mom is eighty-two (82) years of age, widowed
- Mom is currently in a skilled nursing facility in Albany after residing in an assisted living facility in the area where she moved to several years ago from Long Island
- Daughter tells you Mom has $285,000 in the bank

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Our Client (con't.)

- Daughter tells you Mom receives $1,805 of Social Security and $500 of pension payments each month
- Daughter tells you that it will cost $385 per day
  - You know that this facility charges $385 PLUS the 6.8%; remember – the nursing home assessment is part of the applicant's overall monthly medical expenses and can be claimed on the individual's personal income tax return for the year (see New York State Department of Taxation Form IT-258)

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Our Client (con't.)

- You review old notes and inquire as to whether the 529 Plan that Mom set up for grandchild has been transferred; Daughter "forgot" about it and calls you later to confirm it is valued at $11,259
- You also inquire as to Mom's life insurance policy, and later learn it has CSV of $14,545
- You also ascertain that Daughter just paid the October nursing home bill before seeing you

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The Well-Prepared Daughter

- Because you met with Daughter several months ago, she has been gathering financial records for you
- Daughter leaves what she believes is 60 months of records with you and your team begin reviewing
- Daughter also says she has an invoice due for Mom's physical therapy for $3,500

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Initial Marching Orders to Daughter

- You instruct Daughter to:

1. Spend $2,500 on legal fees for your Medicaid Application and your Promissory Note/Gift Plan
2. Spend an additional $2,500 on a preneed funeral arrangement
3. Spend $3,500 on physical therapy bill

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Discoveries

- Your review reveals $13,000 of prior transfers that Daughter cannot explain
- Your review also shows that the $285,000 Daughter thought Mom includes a $125,000 IRA

$285,000 - $125,000 = $160,000 nonqualified funds

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Discoveries

- Your review also reveals that Mom's pension pays a 13th monthly payment, bringing Mom's actual monthly pension to $541.67

$500 x 13 = $6,500 ÷ 12 = $541.67 per month

- Mom takes RMDs out of her IRA equaling $7,310 per year each December

$7,310 ÷ 12 = $609.17 per month income from IRA

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Discoveries

- Your review also reveals $597 of health insurance premiums paid each quarter

$597 ÷ 3 = $199 per month

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Mom's Countable Income

$1,805.00	Social Security
$541.67	Pension
$609.17	IRA
($199.00)	Health Insurance Premium
$2,756.84	

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Mom's Assets

$ 160,000.00	Cash in the bank
$ 11,259.00	value of 529 plan
$ 14,545.00	Life Insurance cash value
$ 185,804.00	Mom's Assets

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Mom's Liabilities

$ 3,500.00	physical therapy bill
$ 2,500.00	Legal fees due
$ 2,500.00	Preneed funeral
$ 8,500.00	

- ** Other ways to handle the physical therapy bill?
- ** What about the penalty for withdrawing 529?

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Mom's Liabilities (con't.)

- Physical therapy bill **may be** needed to offset excess of life insurance if we are unable to liquidate the life insurance in enough time
  - *Unlikely in this plan, because October nursing home bill is paid up*
- We may choose to use entire value of life insurance as portion of gift (particularly if death benefit exceeds cash surrender value by a significant amount)
- In the end, the physical therapy bill has to get paid, so use it wisely

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Mom's Liabilities (con't.)

- 529 Plans are considered assets of the owner (Mom) and the value is the current value minus any charges or deductions imposed to liquidate (10% in most cases); see MRG page 315
- However, we may elect to transfer entire value of plan as part of the gift
  - Depending upon your county, they may count the entire $11,259 as gift or may only count 90% of it as part of the gift

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Mom's Countable Assets

$185,804.00	Mom's Assets
$13,000.00	Prior Gifts
($8,500.00)	Expenses to be paid
$190,304.00	Funds with which to begin our plan

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Prior Gifts

- The prior gift of $13,000 must be added back into the plan; this is often confusing for the client to understand. However, if we pretend that the gift was returned and is now cash in the bank, we would then have that $13,000 to plan with

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Otherwise Eligible Date

- The gift-note plan will be put in place in October, but the "otherwise eligible" determination date of November 1, 2014.
- In our case, we know we'll be private pay through November 1 due to month of October already being paid; however, other times we are "guessing" when Medicare will cut off

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How Much Can Our Note Pay?

- Figure out the maximum Note payment that can occur…*Because eligibility occurs when medical expenses exceed income, Mom's total combined income, including Note payment, cannot exceed cost of care*
- November has 30 days, so the total cost of care for November will be $12,335.40

$385 per day plus 6.8% ($26.18) = $411.18 per day

$411.18 per day x 30 days = $12,335.40

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Maximum Note Payment

- $12,335.40 cost of care minus $2,756.84 of other income = $9,578.56
- Therefore, the MAXIMUM that the Note can pay out is $9,578.55 per month
- NOTE: if your Note were to start on 31-day month, you would have to ensure your total income (Other Income plus Note) did not total more than $12,746.58 ($411.18 x 31)
- February causes big problems…consider waiting until March

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Promissory Notes (con't.)

- Knowing the maximum payout our Note can have, let's play with some figures
- Gift away $86,000.00, results in 9.34 month penalty period

  $86,000÷ 9,212 = 9.34 months
- Loan away $93,900
  - Payable for 10 months at 3.25% interest
  - Generates monthly payment of $9,530.44

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The Loan

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	Enter Values
Loan Amount	$93,900.00
Annual Interest Rate	3.25%
Loan Period in Years	0.8333
Start Date of Loan	10/15/2012

Monthly Payment	$9,530.44
Number of Payments	10
Total Interest	$1,404.39
Total Cost of Loan	$95,304.39

No.	Payment Date	Beginning Balance	Payment	Principal	Interest	Ending Balance
1	11/15/2014	$ 93,900.00	$ 9,530.44	$ 9,276.13	$ 254.31	$ 84,623.87
2	12/15/2014	84,623.87	9,530.44	9,301.25	229.19	75,322.62
3	1/15/2015	75,322.62	9,530.44	9,326.44	204.00	65,996.18
4	2/15/2015	65,996.18	9,530.44	9,351.70	178.74	56,644.48
5	3/15/2015	56,644.48	9,530.44	9,377.03	153.41	47,267.46
6	4/15/2015	47,267.46	9,530.44	9,402.42	128.02	37,865.03
7	5/15/2015	37,865.03	9,530.44	9,427.89	102.55	28,437.14
8	6/15/2015	28,437.14	9,530.44	9,453.42	77.02	18,983.72
9	7/15/2015	18,983.72	9,530.44	9,479.03	51.41	9,504.70
10	8/15/2015	9,504.70	9,530.44	9,504.70	25.74	(0.00)

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Promissory Notes (con't.)

$190,304.00	Assets to begin plan
$86,000.00	Gift
<u>($93,900.00)</u>	Loan
$10,404.00	Assets remaining in Mom's name

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Summary

	Month/Year	# of Days	Daily Rate	Total Cost of NH	Other Income	Note Payment	Deficit
1	November 1, 2014	30	$411.18	$12,335.40	($2,756.84)	($9,530.44)	$48.12
2	December 1, 2014	31	$411.18	$12,746.58	($2,756.84)	($9,530.44)	$459.30
3	January 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,530.44)	$459.30
4	February 1, 2015	28	$411.18	$11,513.04	($2,756.84)	($9,530.44)	($774.24)
5	March 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,530.44)	$459.30
6	April 1, 2015	30	$411.18	$12,335.40	($2,756.84)	($9,530.44)	$48.12
7	May 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,530.44)	$459.30
8	June 1, 2015	30	$411.18	$12,335.40	($2,756.84)	($9,530.44)	$48.12
9	July 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,530.44)	$459.30
10	August 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,530.44)	$459.30
							$2,125.92

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Mom's Assets

$10,404.00	Assets in Mom's name
($2,125.92)	Deficit over 10 month plan
$8,278.08	Assets remaining in Mom's name

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What to Gift?

- The gift IS NOT $86,000
- Remember, we added $13,000 back in to account for prior gifts
- Therefore, direct the client to gift away ONLY $73,000 in additional funds

$86,000 total gift - $13,000 already gifted = $73,000 additional gift to be made now

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What to Gift? (con't.)

$73,000.00	total current gift
($11,259.00)	gift 529 plan
($14,545.00)	gift life insurance
$46,596.00	additional cash to be gifted

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Promissory Notes Discussion Points

- What is the appropriate rate of interest? Test your county…we use 3.25% because we were successful with that when we started years ago; other practitioners use the short or mid-term rate; others demonstrate what a comparable CD rate for a similar duration might pay

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Promissory Notes Discussion Points

- When does the loan start repaying? We'd like to be able to wait a full month before paying, because if you took a loan from a bank, you wouldn't have to make a payment in the first month; however, clients and nursing homes aren't really interested in waiting to be paid!

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Promissory Notes Discussion Points

- Not all gifts are neat and clean; if the Note works out perfectly (not in our case), then the penalty is the same as the length of the loan; most often, that's not the case
- Two options: either extend your loan for the full month OR prepare client for the fact that in the month in which the partial month penalty is due, client will have to contribute toward the cost of care, in addition to regular income
  - For example, if the partial month penalty is .34, the contribution will be $9,212 x .34 = $3,132.08

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Promissory Notes Discussion Points

- What level of retained funds?
  - Some plans work out where A/R has "mid-range" retained funds (as in this example); however, others have A/R retaining very small and others have A/R bumping up against $14,550
  - Mom can apply for income tax refund if she incurred income tax and has medical expenses to offset
  - Mom will apply for partial credit of nursing home assessment

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We Have Achieved "Otherwise Eligible" Status

- This plan works because in November 2014, the A/R is "otherwise eligible" and the penalty period will begin to run for the $86,000 gift that was made.
- February really can throw a wrench in the plan – for good or for bad…be careful that the surplus does not push the A/R over the $14,550 level; watch that refunds and other influxes do not do the same

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Summary

- Total Gift to Daughter of $86,000 will need to be reduced by the interest charged on the loan ($1,404.39)

  $86,000.00 - $1,404.39 = $84,595.61

- Retained funds of $10,404 will be reduced by deficit of $2,125.92

  $10,404 .00 -$2,125.92 = $8,278.08

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Assets Remaining

- Assets Remaining =

$86,000.00	gifted funds
($1,404.39)	interest paid from gift
$10,404.00	countable assets in Mom's name
($2,125.92)	deficit over course of 10 month
$92,873.69	

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Twist

- Assume the same facts, but with a December 1, 2014 start date
- Looks different; result is nearly the same
- Maximum Note payment is now $9,989.73

  $411.18 x 31 = $12,746.58 - $2,756.84 = $9,989.74

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Twist

- Make a gift of $86,400.00 resulting in 9.37 month penalty period
- Loan $88,000.00 over 9 months, paying $9,895.82 per month

$190,304.00	Assets to begin plan
($88,304.00)	Gift
($88,000.00)	Loan
$14,000.00	Assets remaining in Mom's name

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Twist (con't.)

	Enter Values
Loan Amount	$88,000.00
Annual Interest Rate	3.25%
Loan Period in Years	5
Start Date of Loan	10/15/2012

Monthly Payment	$9,910.66
Number of Payments	9
Total Interest	$1,195.96
Total Cost of Loan	$89,195.96

No.	Payment Date	Beginning Balance	Payment	Principal	Interest	Ending Balance
1	10/15/2012	$ 88,000.00	$ 9,910.66	$ 9,672.33	$ 238.33	$ 78,327.67
2	11/15/2012	78,327.67	9,910.66	9,698.53	212.14	68,629.15
3	12/15/2012	68,629.15	9,910.66	9,724.79	185.87	58,904.35
4	1/15/2013	58,904.35	9,910.66	9,751.13	159.53	49,153.22
5	2/15/2013	49,153.22	9,910.66	9,777.54	133.12	39,375.68
6	3/15/2013	39,375.68	9,910.66	9,804.02	106.64	29,571.66
7	4/15/2013	29,571.66	9,910.66	9,830.57	80.09	19,741.09
8	5/15/2013	19,741.09	9,910.66	9,857.20	53.47	9,883.89
9	6/15/2013	9,883.89	9,910.66	9,883.89	26.77	(0.00)

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Summary

	Month/Year	# of Days	Daily Rate	Total Cost of NH	Other Income	Note Payment	Deficit
1	December 1, 2014	31	$411.18	$12,746.58	($2,756.84)	($9,895.82)	$93.92
2	January 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,895.82)	$93.92
3	February 1, 2015	28	$411.18	$11,513.04	($2,756.84)	($9,895.82)	($1,139.62)
4	March 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,895.82)	$93.92
5	April 1, 2015	30	$411.18	$12,335.40	($2,756.84)	($9,895.82)	($317.26)
6	May 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,895.82)	$93.92
7	June 1, 2015	30	$411.18	$12,335.40	($2,756.84)	($9,895.82)	($317.26)
8	July 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,895.82)	$93.92
9	August 1, 2015	31	$411.18	$12,746.58	($2,756.84)	($9,895.82)	$93.92
10	September 1, 2015	30	$411.18	$12,335.40	($2,756.84)	($9,895.82)	($317.26)
							($1,527.88)

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Summary

- This works because, as of December 1st, the income is less than the medical expenses and the penalty period begins to run
- Mom accumulates income over the course of the note due to the "deficit" actually being a "surplus"

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Summary

- Total Gift to Daughter = the $86,400 will need to be reduced by the interest on the loan ($1,195.96)

  $86,400.00 - $1,195.96 interest = $85,204.04

- Retained Funds of $14,000.00 will grow by surplus of $1,527.88
  - This will cause a problem; there may be additional funds received over time; Mom must spend money legitimately

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Assets Remaining

- Assets Remaining:

$	86,400.00	gift
-	1,195.96	interest
+	14,000.00	Mom's assets
+	1,527.88	surplus from loan
$	100,731.92	** spending must occur

to keep Mom below the $14,550 level

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Compare

- Assets Remaining in November 1 plan: $92,649.95
- Assets Remaining in December 1 plan: $110,731.92 (subject to spending)
- *Consider*: is there a RISK by having a surplus over the life of the loan? If end result is almost the same, is it worth having a surplus?

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Conclusion

- Preparation is key
- Managing client's expectations is necessary
- Give yourself a "cushion" in case client calls you and discovers other things
- Give yourself a "cushion" in case DSS finds other transfers

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Conclusion

- Income tax refund; deficit/surplus; and Nursing Home Assessment credit/refund will impact figures
- Remember, retained funds or gifted funds can be used after eligibility for other items (beyond what the $50 Personal Needs Allowance might allow)

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Thank You!

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