IRREVOCABLE TRUSTS: TAKING CARE OF YOURSELF *AND* YOUR RETIREMENT

Many people do not consider protecting assets for future long-term-care costs until they, or their spouse, requires skilled nursing care. Others are aware of the high price of such care (in some cases more than $10,000 a month) but believe that they have saved enough in retirement to defray the cost. In either case, it is a mistake to not consider planning for such costs as a component of an estate plan. A lack of such planning can result in the total depletion of a person's assets, which they worked hard to earn and save throughout their lifetime. Particularly so since some people spend *years* of their lives in nursing homes.

Planning for long-term-care typically involves the creation of an irrevocable trust. The technique is to transfer assets to the trust, of which the creator of the trust (known as the grantor) is, generally, not a beneficiary. After a five-year period has elapsed, should the grantor require skilled nursing, the assets contained within the trust will not be reported on a Medicaid application. The term "five year lookback" refers to the State's ability to review an applicant's financial records for the sixty months prior to the date of the application to determine whether the applicant has transferred any assets of value without consideration – in other words, to determine whether the applicant has made any gifts. If the applicant has indeed made a gift, the State will deny the Medicaid application until a so-called "penalty period" has expired. The penalty period is the amount of months calculated by taking the amount of the gift and dividing it by a number called the "penalty divisor," slightly north of $9,000 for 2020. For this reason, the earlier a person creates and funds an irrevocable trust, the better.

While the word "irrevocable" may conjure up feelings of anxiety, estate planners can build in some flexibility. For starters, the grantors of the trust can also serve as the trustees, making investment and distribution decisions. The trusts can also be "income tax defective" such that gains within the trust are paid by the grantor at the lower, individual income tax rates, rather than at the higher trust tax rates. While grantors cannot be beneficiaries of the principal, irrevocable nursing home trusts can be drafted so as to allow for distributions of income to the grantors. Bear in mind, however, that this exposes the income to nursing home costs. Also, the grantors' family can be the beneficiaries of the trust – children, grandchildren, parents and siblings. What this means is that grantors can make distributions to family members and ask for the money back, in the event the grantors find that they have overfunded the trust. However, it is important to recognize that the beneficiaries cannot be under any legal obligation to give the money back. Having a side agreement with the beneficiaries requiring them to refund any money distributed would result in the assets of the trust being countable resources for Medicaid purposes.

Real property is an ideal asset to transfer into an irrevocable trust as grantors can reserve a life estate in the deed and continue to live in the property. Similarly, grantors and trustees can enter into occupancy agreements concerning investment properties transferred into an irrevocable trust. Real property can be sold from the Trust with the proceeds deposited into the Trust account. Importantly, selling real estate and depositing the proceeds does not re-trigger the five-year clock. The clock continues to run and does not reset.

Irrevocable trusts have many additional benefits, beyond protecting assets from nursing home costs and preserving wealth for future generations. As with other trusts, irrevocable trusts are will alternatives, transferring assets to future generations without the need to pass the assets through the probate process. Probate is a court process that must be used when a person passes owning assets in his or her name. It is time-consuming, expensive and results in a complete lack of privacy. The *terms* of irrevocable trusts can provide protection for beneficiaries by reducing and/or eliminating the possibility that a third-party such as a divorcing spouse, business creditor, consumer creditor or personal injury claim creditor can satisfy a judgment against the beneficiary from his or her share of the trust estate. Further, if the grantors have children or grandchildren with special needs, the irrevocable trust can include terms so as to prevent disqualification of the special needs beneficiary from governmental benefits upon the death of the grantor.

No estate plan should be finalized until the planning for the cost of long-term-care is thought through. Please contact PLDO Trust and Estate Partner Rebecca M. Murphy for further information at 401-824-5100 or email rmurphy@pldolaw.com.

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