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**Income Only Trusts:
Medicaid, VA and Tax
Planning
Considerations**

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Today's Topics

- Structure of IIOT's
- Medicaid Planning
- Veterans Benefit Planning
- Tax Considerations

Background

- For MA planning, historically used for asset protection for LTC.
- Variety of other benefits with careful drafting
- Post DRA popularity

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IIOT Creation

- Self Settled
- By MA applicant or spouse

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Choosing Trustee

- Usually child of Settlor
- May be Settlor
 - Not prohibited by any MA rule
- Fiduciary capacity
- Remainder interest vested in remainder beneficiaries

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Irrevocability

- Must be Irrevocable
- Cannot be revoked unilaterally by Settlor
- UTA allows termination/amendment by agreement of interested parties

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Income Payments

- May be Retained by Settlor or spouse for life
- Discretionary distributions to remainder bene's
- Vs. Capital Gains

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Principal Distributions

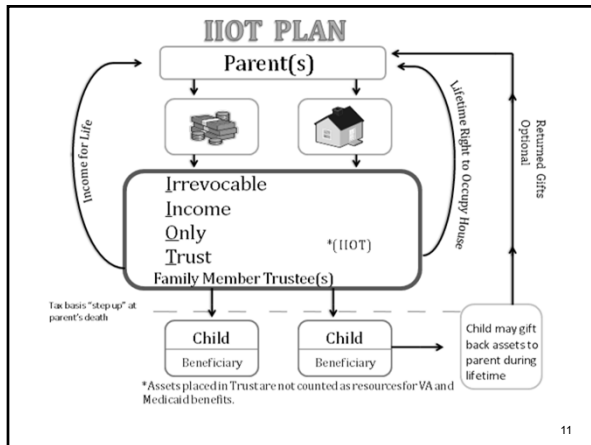
- May not go to Settlor
- May be retained, or
- Paid to remainder bene's at Trustee's discretion

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Payments at Death

- Income may continue to Settlor's spouse
- Principal to remainder beneficiaries or in further trust for bene's other than Settlor's spouse or estate

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Medicaid Issues

- Transfer to Trust is gift subject to penalty for 5 years.
- No penalty for transfers from trust to bene's

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Medicaid Treatment

- Permitted by OBRA '93
- CMS Clarification: "If no portion of the trust corpus can be distributed to an individual, then no portion of the trust is deemed a resource of the individual for Medicaid eligibility purposes"

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Principal "Back Door"

- Settlor cannot access principal, but
- Termination by all parties
- Distribution to remainder bene's who may voluntarily use for benefit of Settlor

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Funding

- Appreciated liquid investments
- Real Estate
- Can maintain IRC 121

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VA / MA Issues

- Integrate VA and MA planning issues
- Currently no transfer penalty for VA benefits

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Veterans Benefits

- Assets transferred to IIOT not considered countable resources unless actually distributed to applicant

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VA Issues

- Disclosure of trust to VA
- Sale of home in IIOT
- Income vs. Capital Gains Tax Reporting
- Watch income vs. UME's

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Income Tax Issues

- Income taxed to Settlor
- Do not need EIN
- Income available for MA eligibility
- VA may count income

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Grantor Trust

- Step up in basis to DOD value
- Retain Ltd. Power of appointment
- Retain Income, etc.
- Avoids trust tax rates

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Estate / Gift Tax

- Trust value included in decedent's estate for FET purposes
- Incomplete gift so no gift tax applied at funding

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Estate Recovery

- Trust assets not subject to probate, so not included in MAER in under current program.

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Other Advantages

- Settlor control of ultimate distributions
- Creditor protection
- Preserve Financial Aid for Grandchildren

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Questions?

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Conclusion

- More than just Medicaid planning
- Drafting to maximize tax treatment tricky

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