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Use of Irrevocable Annuities to Qualify a Member of a Married Couple for MassHealth

Irrevocable annuities are often used where a member of a married couple wishes to qualify for MassHealth coverage (in-home or nursing home), but the couple's countable assets exceed the permitted \$148,620 (2023). An applicant is limited to \$2,000 in assets and the applicant's spouse is limited to \$126,420, in addition to a principal residence (and any contiguous parcels) of any value and one automobile. The combined \$148,620 typically consists of bank accounts, retirement accounts, investment accounts, a second vehicle, and/or cash value of life insurance. It may also include the value of a second parcel of non-contiguous real estate, so long as all of the countable assets total less than \$148,620.

Additional real estate which exceeds the \$148,620 is generally countable (resulting in excess assets), but may be considered non-countable if it is rental property with a net profit or, if it is not income-producing, the non-applicant spouse has signed a MassHealth Agreement to Sell, which requires that the property be listed with a real estate agent and efforts made to sell it within nine (9) months. Our recommendation is to wait until as far into the MassHealth process as possible to sign a listing agreement with a real estate agent, to avoid sale closing before MassHealth benefits are approved, in which case the cash proceeds will put the couple back over the \$148,620 and, at that point, there will be limited options for how to protect them. MassHealth has not been active in following-up on cases where an Agreement to Sell has been signed, so a property can often remain on the market will past the nine (9)-month deadline without any negative ramifications.

In cases where the non-applicant spouse has more assets than permitted, there are typically two options for spending down the excess:

1) purchase two irrevocable pre-paid funeral contracts, open two \$1,500 burial savings accounts, and/or pay privately for care, until the combined countable assets are reduced to \$148,620; or

2) place the excess funds (over the \$148,620) in a MassHealth-qualifying annuity. This can be done without pre-paying funerals or opening burial savings accounts, but some families elect to do both, simply for the peace of mind of knowing that funeral

arrangements have been taken care of and it means fewer assets are placed in the annuity.

Naturally, most people elect the second option, since it increases the chances that the couple's assets will be preserved. This article explains how annuities work in the MassHealth context.

An annuity is a contract with an insurance company under which the owner (in this case, the applicant's spouse) pays the insurance company a sum of money in exchange for a stream of income. This income is paid monthly for a specific number of years. To avoid a transfer penalty, the annuity must meet the following criteria:

- Payments must begin immediately (they cannot be deferred).
- The entire investment must be returned over the term of the contract, in equal payments.
- The payment period may not exceed the owner's life expectancy under the Social Security tables. For instance, if the spouse's life expectancy is four (4) years, the purchase of an annuity with a six (6)-year payback period would be deemed a transfer of assets and disqualify the applicant for a particular period of time (based upon the value of the "extra" two years).
- The annuity must be irrevocable and nontransferable, meaning that the owner may not have the option of cashing it out and/or selling it to a third party.
- As a result of the Massachusetts Supreme Judicial Court decision in *Dermody v. EOHHS and Nationwide*, issued January 27, 2023, the annuity must name the Commonwealth of Massachusetts as the primary beneficiary of any funds remaining, if the annuity owner dies before all the payments have been made. Our office recommends language reading, "**Commonwealth of Massachusetts, to the extent of benefits paid to the institutionalized individual.**" Although some MassHealth caseworkers might want the language to refer to "individuals," to cover both spouses, this addition is inconsistent with the regulation. This reflects the fact that MassHealth has taken the position that it can be reimbursed for any benefits paid for either the nursing home spouse or the annuitant spouse. Any remaining funds after MassHealth has been reimbursed may be payable to the contingent beneficiary of the owner's choice (often, children of the annuitant, but, ideally, a revocable trust, whose terms may be modified, because the annuity contract does not allow for changing the beneficiary).

For example, if Mike and Louise are married and Mike needs either in-home or skilled-nursing home care, the couple's combined assets will be considered when determining if Mike is eligible for MassHealth benefits to assist with the cost. If their cash assets (bank, retirement and investment accounts, shares of stock, cash surrender value of life insurance, and any second car or parcel of real estate) exceed \$148,620, Louise does not have to spend the excess on Mike's care. Instead, she could purchase an annuity with all funds over the \$148,620.

After careful analysis of how many assets exceed the \$148,620 and which assets are best used to purchase an annuity, so as to minimize income taxes, Louise would obtain

a bank check (not a personal check), so that the funds would be immediately debited from her account) payable to the annuity company, in the amount of the excess funds. The date on the bank check establishes Mike's first day of MassHealth eligibility: the following day. Once the check is obtained, Louise will meet with an insurance agent to complete all forms necessary to purchase the annuity. If some of the assets needed to purchase the annuity are Louise's retirement accounts, she might have two annuities – one purchased with non-retirement funds (reflected in the bank check) and one with funds rolled over (electronically) from an IRA into a special annuity intended for tax-deferred assets. Although Mike's retirement accounts would need to be liquidated (and income taxes paid), Louise can avoid paying any income taxes by rolling her accounts into an annuity (she will be taxed only as the payments are made to her).

To satisfy the MassHealth regulations, Louise must name the Commonwealth of Massachusetts as primary beneficiary of the annuity (to receive any funds remaining on her death, to the extent MassHealth benefits were paid out for either her or Mike). She may designate the contingent beneficiary of her choice. Since the annuity is irrevocable, she must be careful to designate the correct beneficiaries (they cannot be changed later).

Although Louise is welcome to name her children as contingent beneficiaries (for any funds remaining after the Commonwealth's claim), she cannot change this if circumstances arise which support making a change. For example, if one of her children predeceases her, it is likely that the annuity company would pay any balance to her surviving children, rather than to the children of Louise's deceased child. Or, if one of her children became disabled and inheriting funds would jeopardize that child's eligibility for public benefits, it would be preferable to direct that child's share to a trust. Therefore, one option is for Louise to execute a revocable trust detailing her wishes about who would inherit any remaining funds and what would happen to the share of a deceased child. She could name the trust as contingent beneficiary (rather than her children) and know that the terms of the trust could be changed at any time, if circumstances warranted it. This is a wonderful way to give Louise flexibility in who would inherit any leftover funds, if she died before all payments were made to her. Note that any trust must be signed before Louise purchases the annuity.

Once the annuity paperwork has been completed and filed with the annuity company, there is no rush to file the MassHealth application. The date of eligibility has been set and Louise has until the end of the third month after that date to file for MassHealth, while preserving Mike's ability to obtain coverage retroactively to the date after the check. For example, if Louise obtain a bank check in the amount of her excess assets on June 12th, she has until September 30th to file the MassHealth application. Assuming she was successful in reducing her assets and there are no disqualifying transfers of assets in the prior 60 months, she can be assured of Mike's eligibility date.

Once the annuity contract has been issued (several weeks later), Louise will start receiving checks every month for the term of the annuity. For example, if she put \$150,000 in the annuity for a 60-month term, she would receive a check for approximately \$2,500 each month. She should not deposit any of the checks until Mike's MassHealth benefits have been approved. If she deposits them before approval, she risks having

assets exceeding the \$148,620. Most MassHealth workers will be satisfied that she has reduced her assets to \$148,620 on the date she obtained the bank check and approve Mike's application based upon that fact, but a few will insist on verification months later, showing that Louise's assets are still under the \$148,620. It is not worth taking the risk that Louise's assets will be revisited, so, even though it may be difficult, the checks should remain undeposited until benefits haven been approved. After approval, they may be deposited and Louise may work with the insurance agent to arrange for direct deposit of all future payments. Once Mike's MassHealth eligibility has been determined, MassHealth may no longer request information on Louise's assets.

If Louise lives beyond the period of the annuity (typically 4-5 years), she will recover all of the payments and, possibly, a small amount of interest (in this situation, the annuity is not intended to produce a favorable return – it is simply a strategy to preserve principal). As the checks arrive, she may invest them however she wishes – in the bank, in an investment account, or purchasing shares of stock.

However, if Louise dies before all of the funds have been returned to her, the annuity company must contact MassHealth to determine the total paid for Mike's care (or for any coverage Louise might have had). MassHealth is entitled to the balance of the unpaid funds and Louise's children will receive any remaining funds. If MassHealth paid out more benefits that are in the annuity, they cannot seek reimbursement from any other source (Louise and Mike's children, for example) – MassHealth may have only what remains in the annuity. Of course, the best advice for Louise is to be sure to outlive the annuity, so that all funds are re-paid to her and nothing will be available for MassHealth.

Some considerations when deciding whether to purchase an annuity:

- 1) There may be significant income taxes due as a result of liquidating the MassHealth applicant's retirement accounts, but remember that income taxes would be due at some point – it is simply that they are being incurred all at one time, with some of the proceeds possibly subject to slightly higher taxes (if they bump the couple's income into a higher tax bracket).
- 2) The non-applicant spouse who purchases the annuity and receives all of the payments, may become ill, in which case the monthly payments and the accumulated funds would be at risk to that spouse's at-home or nursing home expenses.
- 3) If the non-applicant spouse dies before all of the funds are returned and MassHealth makes a claim against the remaining principal, know that what MassHealth paid for the spouse's care is generally much less than if the couple had not purchased the annuity and, instead, paid privately. MassHealth has contract rates with each facility which dictate how much the facility will receive each month on behalf of the residents on MassHealth. That figure is typically between approximately \$6,200 and \$7,000. The resident's income is applied toward that sum and MassHealth pays the rest. Depending upon how much income the nursing home spouse has, MassHealth may pay only a few thousand dollars a month. Therefore, the family benefits from this lower rate and reimburses

MassHealth for much less than if the couple had paid privately. Savings may be as much as \$10,000/month.

- 4) In some cases, the savings may be small due to a high income or the short life expectancy of the nursing home spouse, and the process of liquidating assets and applying for Medicaid might not be worth the considerable trouble.
- 5) Unless the annuity is for a significant sum, there are minimal earnings. Annuities are purchased to preserve the principal, not to earn interest.
- 6) Although MassHealth regulations do not state a limit on the level of assets which a couple can invest in an annuity, many attorneys have their personal limits, beyond which the purchase may be considered abusive.
- 7) Since only the applicant's income is considered available for MassHealth, the non-applicant spouse is entitled to keep all of the annuity checks.
- 8) In some rare cases, where the non-applicant spouse's income is relatively low, it may not make sense to purchase an annuity.
- 9) Many financial planners and insurance agents will be eager to sell annuities (because of the commission), but be certain that the individual you work with has experience in issuing MassHealth-compliant annuities. We have had problems where we used our clients' personal agent, including one where we had to contact the Massachusetts Division of Insurance for assistance in correcting a botched policy. We now insist that clients who work with our office use one of the agents we know and trust.

This is intended to be a general description of the process of using irrevocable annuities to qualify one member of a married couple for in-home and skilled-nursing MassHealth coverage, but individual circumstances may permit other methods of obtaining eligibility or may limit eligibility. Because each situation is different and the laws relating to MassHealth eligibility are regularly changing, a competent elder law attorney should be consulted concerning any particular situation and legal advice relative to these issues. This article was updated on May 5, 2023 and is for informational purposes only and not intended to constitute comprehensive or specific legal advice.