

VETERANS BENEFITS PLANNING: THE NEW LOOKBACK AND NET WORTH RULES

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ABOUT THE AUTHOR

Evan Farr is the creator of the **Living Trust Plus™ Asset Protection System** used by dozens of Estate Planning and Elder Law Attorneys around the country, and is widely recognized as one of the foremost experts in the Country in the field of Medicaid Asset Protection and related Trusts. Evan is both a Certified Elder Law Attorney through the National Elder Law Foundation and a Member of NAELA's Council of Advanced Practitioners. Evan has been quoted or cited as an expert by numerous sources, including the *Washington Post*, *Newsweek Magazine*, *Northern Virginia Magazine*, *Trusts & Estates Magazine*, *The American Institute of Certified Public Accountants*, and the American Bar Association, and has been featured as a guest speaker on numerous radio shows, including WTOP and Washington Post Radio.

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Note: This outline is intended to educate and assist readers, but does not constitute legal advice. Readers should consider carefully the applicability and consequences of using any planning technique. The writer and publisher expressly disclaim (i) all warranties, express and implied, including, without limitation, of merchantability and fitness for any particular purpose, and (ii) all other responsibility for all consequences of use of this material. Virginia has no process for approving certifying organizations.

SECTION 1. VETERAN'S PENSION / AID AND ATTENDANCE

1.1. Basic Overview of Veteran's Pension / Aid and Attendance.

1.1.1. Purpose.

- 1.1.1.1. The Purpose of Veteran's Asset Protection Planning is to protect a wartime veteran's assets in order to qualify the veteran to receive the Veteran's Aid and Attendance special pension benefit to assist the Veteran in paying for long-term care, typically care delivered at home or in an assisted living facility. Of course, like Medicaid, the Veteran's Aid and Attendance special pension benefit has its own complex financial requirements that must be met.

1.1.2. Planning for Eligibility.

- 1.1.2.1. Meeting the financial requirements is often a difficult hurdle for a veteran seeking aid and attendance benefits, and the use of various asset protection strategies, such as half-loaf planning and irrevocable trusts, can provide helpful planning tools.

1.2. The Relevant Law.

1.2.1. United States Code.

- 1.2.1.1. The Department of Veterans Affairs (VA) administers a needs-based benefit, called “pension” (previously called “improved pension”) for wartime veterans and for surviving spouses and children of wartime veterans. The current pension program was established by the Veterans' and Survivors' Pension Improvement Act of 1978, 95, 92 Stat. 2497, and became effective January 1, 1979. The statutory authority for pension is 38 U.S.C. chapter 15, implemented at 38 CFR 3.271 through 3.277.
- 1.2.1.2. The United States Code gives the Secretary of Veterans Affairs the authority to prescribe all rules and regulations which are necessary or appropriate to carry out the laws administered by the Department and are consistent with those laws. (Section 501, Title 38 U.S.C.)
- 1.2.1.3. Under the new **Proposed Rule for Net Worth, Asset Transfers, and Income Exclusions for Needs-Based Benefits**, which can be found online at <http://tinyurl.com/VA-Proposed-Rules>, some terminology is being changed. When specificity is required in VA regulations to distinguish between veterans and survivors, the new rules will refer to “veterans pension” and “survivors pension” instead of “disability pension” and “death pension” as used in the old rule. This is because the VA determined that the term “disability pension” was a misnomer

because a veteran who has attained age 65 does not need to be disabled to receive pension.

1.2.2. Code of Federal Regulations

- 1.2.2.1. As stated above, the statutory authority for veterans pension is 38 U.S.C. chapter 15, implemented at 38 CFR 3.271 through 3.277. The Compensation and Pension Service writes the regulations that pertain to the adjudication of claims for compensation, pension and other benefits that are processed by adjudication personnel. All regulations (proposed and final) are published in the Federal Register. There is an Office of General Counsel that issues written interpretation of the law whenever necessary.

1.2.3. Directives and Records.

- 1.2.3.1. Directives provide instructions to VA personnel. There are different forms of directives but the ones most commonly encountered are Circulars (used when required for special projects, to implement a program with an ending date, to implement instructions subject to frequent change, or to test a procedure) and Manuals (designed to provide procedures for benefit payments and, in general, for all the work everyone in VA does).
- 1.2.3.2. The primary document used for Veterans Aid and Attendance is a Manual – specifically **M21-1: Adjudication Procedures**. See the VA website here for more information: http://www.benefits.va.gov/WARMS/Site_Map.asp.

1.3. Transfers and Look Back.

1.3.1. Look Back Period.

- 1.3.1.1. As of the this writing, the VA does not penalize veterans for transfers of assets and does not yet have a formal “look-back” period, but evaluates the veteran's financial condition at the time of the application.
- 1.3.1.2. However, under the **Proposed Rule for Net Worth, Asset Transfers, and Income Exclusions for Needs-Based Benefits**, which can be found online at <http://tinyurl.com/VA-Proposed-Rules>, the Veterans Administration will be introducing a 36-month lookback rule. The changes will establish a 36-month look-back period and establish a penalty period not to exceed 10 years for those who dispose of assets to qualify for a Veterans special pension. Proposed Rule Section 3.276 will establish a presumption, absent clear and convincing evidence showing otherwise, that asset transfers made during the look-back period were made to establish pension entitlement. The penalty period (defined as a period of non-entitlement due to transfer of a covered asset). will be calculated based on the

total assets transferred during the look-back period to the extent they would have made net worth excessive. **However, the penalty period will begin the first day of the month that follows the last asset transfer, which will provide Elder Law Attorneys with a new Asset Protection Opportunity.** See Section 2.1.

- 1.3.1.3. Proposed § 3.276(a)(7) will define “look-back period” to mean the 36-month period before the date on which VA receives either an original pension claim or a new pension claim after a period of non-entitlement. VA’s new 3-year look-back period is similar to that employed by the Social Security Administration in administering its SSI program. Although Medicaid uses a 5-year look-back period for most transfers of assets, as a policy matter, VA currently believes that a 3-year look-back period is sufficient to preserve the integrity of its pension program.

1.3.2. Transfer Penalty.

- 1.3.2.1. Section 3.276 of the new rules propose a new Penalty Period for Asset Transfers. Proposed § 3.276(a) will define “covered asset,” “covered asset amount,” “fair market value,” “transfer for less than fair market value,” “annuity,” “trust,” “uncompensated value,” “look-back period” and “penalty period.” These definitions will make this complex regulation easier to understand. The proposed rule will also provide a cross-reference to the definition of “claimant” in proposed § 3.275, which would mean claimants, beneficiaries, and dependent spouses, as well as dependent or potentially dependent children.
- 1.3.2.2. Proposed § 3.276(a) will define “covered asset” to mean an asset that was part of net worth, was transferred for less than fair market value, and will have caused or partially caused net worth to exceed the limit had the claimant not transferred the asset. The “covered asset amount” will be the monetary amount by which net worth will have exceeded the limit on account of a covered asset if the uncompensated value of the covered asset had been included in the net worth calculation. These definitions are important because the covered asset amount is the amount that VA proposes to use to calculate the penalty period as described below. A smaller covered asset amount results in a shorter penalty period. The VA has propose to define “covered asset amount” in this manner because, in its view, it would be inequitable to calculate a penalty period using the entire transferred amount when net worth will have exceeded the limit by only a small amount if the claimant had not transferred any assets at all.
- 1.3.2.3. In proposed § 3.276(a)(4), the VA will define “fair market value” as the price at which an asset will change hands between a willing buyer and willing seller who are under no compulsion to buy or sell and who have reasonable knowledge of relevant facts. VA uses the best available information to determine fair market value, such as inspections, appraisals, public records, and the market value of

similar property if applicable. Using the best available information to determine a fair value is a restatement of current and longstanding policy.

- 1.3.2.4. The VA has proposed to define “transfer for less than fair market value” as selling, conveying, gifting, or exchanging an asset for an amount less than the fair market value of the asset. In addition, included as a transfer for less than fair market value will be any asset transfer to or purchase of any financial instrument or investment that reduces net worth and will not be in the claimant's financial interest were it not for the claimant's attempt to qualify for VA pension by transferring assets to or purchasing such instruments or investments.

1.3.2.4.1. Two examples the VA provides of such instruments or investments are **annuities and trusts**.

1.3.2.4.1.1. The VA will define “annuity” to mean “a financial instrument that provides income over a defined period of time for an initial payment of principal.”

1.3.2.4.1.2. The VA will define “trust” to mean a legal arrangement by which an individual (the grantor) transfers property to an individual or an entity (the trustee), who manages the property according to the terms of the trust, whether for the grantor's own benefit or for the benefit of another individual.

1.3.2.4.2. The “uncompensated value” of an asset will be defined as the difference between its fair market value and the amount of compensation an individual receives for the asset. (In this context, the word “compensation” has its more general meaning rather than the technical meaning given in 38 U.S.C. 101(13).) In the case of an asset transfer to, or purchase of, a financial instrument or investment such as a trust or an annuity, the uncompensated value will mean the amount of money or the monetary value of other assets so transferred.

1.3.3. Silver Lining for Attorneys.

- 1.3.3.1. Based on the new definition “uncompensated value,” the purchase of any annuity will be considered an uncompensated transfer, ruling out the use any types of annuities in connection with Veterans Benefits planning. This should actually be good news to most attorneys, as there are a lot of insurance salesmen out there that prey on older Veterans by selling inappropriate annuities that, in the past, may have helped them qualify for the Veterans pension, but in the long run hurt the consumer because these annuities were not compliant for purposes of Medicaid. Accordingly, this new rule will hopefully eliminate this type of predatory practice by these types of insurance salesmen. Instead, clients will turn to experienced Elder Law Attorneys to prepare Medicaid Asset Protection Trusts (discussed in more depth below) that also work to protect assets in connection the Veterans Pension.

1.3.4. Exempt Transfers

1.3.4.1. **Transfers as a Result of Fraud, Misrepresentation, or Unfair Business Practice Related to the Sale or Marketing of Financial Products.** The presumption of an uncompensated transfer can be rebutted if the claimant establishes that he or she transferred an asset as the result of fraud, misrepresentation, or unfair business practice related to the sale or marketing of financial products or services for purposes of establishing entitlement to VA pension. However, the burden of rebutting the presumption is high, as the VA has proposed that evidence substantiating the application of this exception may include a “complaint contemporaneously filed with state, local, or Federal authorities reporting the incident.” In such a case, VA would not consider the transferred asset to be a covered asset and would thus not calculate any penalty period, although this would mean that net worth would be excessive and the provisions of § 3.274 regarding reducing net worth (discussed below) would apply.

1.3.4.1.1. Because of the wording of this proposed regulation, it is unclear whether this new rule will apply to fraud or misrepresentation committed by someone not in the financial industry and related to the to the sale or marketing of financial products. In other words, what if a con man or defrauds a veteran out of money, or a veteran falls prey to a Nigerian scam, Telemarketing Fraud, Advance Fee Schemes, or some other type of common Internet scams?¹ This uncertainty is due to the fact that it is unclear whether the phrase “as the result of fraud, misrepresentation, or unfair business practice related to the sale or marketing of financial products or services for purposes of establishing entitlement to VA pension” is intended to just apply to the sale or marketing of financial products or services for purposes of establishing entitlement to VA pension, or whether the sentence should be read as if the commas were actually semi-colons, *i.e.*: “as the result of fraud; as the result misrepresentation; or as the result of unfair business practice related to the sale or marketing of financial products or services for purposes of establishing entitlement to VA pension.”

1.3.4.2. **Trust for Disabled Child Exception.** Proposed § 3.276(d) will also set forth an exception that applies to assets transferred to a **trust for the benefit of a veteran's child whom VA rates or has rated as being permanently incapable of self-support** under the provision of 38 CFR 3.356. VA would not consider assets transferred to a trust established on behalf of such a child to be covered assets as long as there is no circumstance under which distributions from the trust can be used to benefit the veteran, veteran's spouse, or surviving spouse. Presumably a third-party Special Needs Trust would be one appropriate mechanism for this type of exempt transfer.

¹ See <https://www.fbi.gov/scams-safety/fraud>.

1.3.4.3. **No Hardship Exception.** VA considered providing for an exception consistent with the “undue hardship” determination prescribed in the aforementioned SSI statute, 42 U.S.C. 1382b(c)(1)(C)(iv). However, the statutory resource limit in the SSI program is \$3,000 for an individual with a spouse and \$2,000 for an individual with no spouse. See 42 U.S.C. 1382(a)(3). Because these limits are significantly lower than the net worth limit that VA proposes to use, the VA does not believe that a hardship provision is warranted.

1.4. Amount of the Benefit - Maximum Annual Pension Rate (MAPR).

1.4.1. Aid & Attendance Amounts as of February 2016:

- Single sick Veteran ~ \$21,466 per year / \$1,788 per month
- Healthy Veteran with sick spouse ~ \$16,848 per year / \$1,404 per month
- Married sick Veteran ~ \$25,448 per year / \$2,120 per month
- Married, Both Veterans sick ~ \$34,050 per year / \$2,837 per month
- Surviving Spouse - \$13,794 per year / \$1,149 per month

1.4.2. Calculation of Penalty Period.

1.4.2.1. In § 3.276(e), VA will establish both the penalty period for covered assets transferred during the look-back period and the criteria for calculating the penalty period. In determining the calculations for the length of the penalty period, the VA drew on 42 U.S.C. 1382b(c), pertaining to SSI. Subsection (c)(1)(A)(iv) of 42 U.S.C. 1382b establishes a formula for calculating penalty periods for purposes of SSI. VA's formula will be similar. VA's formula will determine a penalty period in months by dividing the covered asset amount by the applicable maximum annual pension rate under 38 U.S.C. 1521(d), 1541(d), or 1542 as of the date of the pension claim, rounded down to the nearest whole number.

1.4.2.1.1. For both veterans and surviving spouses, the VA will use the Maximum Annual Pension Rate (*see* section 1.4) in effect as of the date of the pension claim, at the Aid and Attendance level. This is good, because the higher the divisor, the shorter the penalty period, despite the fact that not all veterans and surviving spouses to whom the regulation would apply will qualify for pension at the Aid and Attendance level.

1.4.2.1.2. The VA decided to set a maximum penalty period of 10 years. They considered setting the maximum penalty period at 36 months, which would be consistent with the SSI statute; however, after further consideration, they

determined that it would be inequitable for an individual who transfers, for example, \$1,000,000 to have a penalty period of the same length as an individual who transfers \$25,000.

1.4.2.1.3. The VA’s **Summary of Major Provisions** is contradictory as to when the penalty period will start.

1.4.2.1.3.1. In one place in the **Summary of Major Provisions** -- <https://www.federalregister.gov/articles/2015/01/23/2015-00297/net-worth-asset-transfers-and-income-exclusions-for-needs-based-benefits#p-16> -- it says that “[t]he penalty period would begin the first day of the month that follows the last asset transfer.”

1.4.2.1.3.2. In another place in the **Summary of Major Provisions** – <https://www.federalregister.gov/articles/2015/01/23/2015-00297/net-worth-asset-transfers-and-income-exclusions-for-needs-based-benefits#p-81> – it says that “[u]nder proposed § 3.276(e)(2), the penalty period would begin on the date that would have been the payment date of an original or new pension award if the claimant had not transferred a covered asset and the claimant's net worth had been within the limit.” However, this statement in the **Summary** appears to be incorrect, because:

1.4.2.1.3.3. Under the actual proposed § 3.276(e)(2), **the penalty period begins on the first day of the month that follows the date of the transfer.** If there was more than one transfer, **the penalty period will begin on the first day of the month that follows the date of the last transfer.** Under proposed § 3.276(e)(3), the claimant, if otherwise qualified, would then be entitled to pension benefits effective the last day of the last month of the penalty period, with a payment date as of the first day of the following month in accordance with 38 CFR 3.31.

1.4.2.1.4. **Examples of Penalty Periods:**

1.4.2.1.4.1. Married Couple with Sick Veteran

Married Veteran Penalty Divisor:	\$2,120
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Amount Transferred	÷	2120	=	Number of Months Disqualified	Rounded Down to Nearest Whole Number
\$50,000.00	÷	2120	=	23.6	23.0
\$75,000.00	÷	2120	=	35.4	35.0

\$100,000.00	÷	2120	=	47.2	47.0
\$150,000.00	÷	2120	=	70.8	70.0
\$250,000.00	÷	2120	=	117.9	117.0
\$255,000.00 or up	÷	2120	=	120 (maximum number of months)	120.0

1.4.2.1.4.2. Single Veteran

Single Veteran Penalty Divisor:	\$1,788
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Amount Transferred	÷	1788	=	Number of Months Disqualified	Rounded Down to Nearest Whole Number
\$64,000.00	÷	1788	=	35.8	35.0
\$100,000.00	÷	1788	=	55.9	55.0
\$150,000.00	÷	1788	=	83.9	83.0
\$200,000.00	÷	1788	=	111.9	111.0
\$215,000.00 or up	÷	1788	=	120 (maximum number of months)	120.0

1.4.2.1.4.3. As you can see from the above examples, the penalty periods that will be imposed by the VA under the new regulations will result in periods well in excess of 3 years except for the smallest transfers (less than \$75,000 for a married veteran and less than \$64,000 for a single veteran).

1.4.3. No Recalculation of Penalty Period.

1.4.3.1. Proposed § 3.276(e)(5) states that, with two exceptions, VA would not recalculate a penalty period under this section. VA would recalculate the penalty period if:

1.4.3.1.1. the original calculation is shown to be erroneous, or

1.4.3.1.2. **all** of the covered assets were returned to the claimant before the date of claim or within 30 days after the date of claim. If, not later than 90 days after VA's decision notice pertaining to the penalty period, VA receives evidence

showing that all covered assets have been returned to the claimant, VA would not assess a penalty period. Although VA would not assess a penalty period in such a situation, the claimant's net worth would be excessive, but would be available for the claimant to use for his or her needs consistent with Congressional intent.

- 1.4.3.2. **Transfer and Cure Does Not Work.** Unlike with the Medicaid Transfer and cure strategy, once a VA penalty period has been correctly calculated, the penalty period would be fixed, and return of covered assets after the 30-day period provided would not shorten the penalty period. The VA reasons that “numerous penalty period recalculations would detract from the primary mission of paying pension benefits to those in need.”

1.5. Who Is Eligible?

1.5.1. Service Eligibility.

- 1.5.1.1. To receive the Veterans Aid & Attendance Special Pension Benefit, or the Housebound Special Pension Benefit, which is similar but pays less than Aid & Attendance (hereinafter I will refer to both of these benefits as the “Veterans Pension”), a veteran must have served on active duty, at least 90 days, at least one day of which occurred during a period designated as wartime:
 - 1.5.1.2. World War II: December 7, 1941 through December 31, 1946.
 - 1.5.1.3. Korean Conflict: June 27, 1950 through January 31, 1955.
 - 1.5.1.4. Vietnam Era: August 5, 1964 through May 7, 1975; for veterans who served “in country” before August 5, 1964 the dates are February 28, 1961 through May 7, 1975.
 - 1.5.1.5. Gulf War: August 2, 1990 through a date to be set by law or Presidential Proclamation
 - 1.5.1.6. There must have been an honorable discharge. Single surviving spouses of such veterans are also eligible.
 - 1.5.1.7. If the claimant is under 65, the applicant must be totally disabled.
 - 1.5.1.8. If the claimant is at least 65, there is no requirement to prove disability. However, the veteran or spouse must be in need of regular aid and attendance due to: Inability of claimant to dress or undress himself/herself, or to keep himself/herself ordinarily clean and presentable; frequent need of adjustment of any special prosthetic or orthopedic appliances which by

reason of the particular disability cannot be done without aid (this will not include the adjustment of appliances which normal persons would be unable to adjust without aid, such as supports, belts, lacing at the back etc.); inability to feed himself/herself through loss of coordination of upper extremities or through extreme weakness; inability to attend to the wants of nature; or incapacity, physical or mental, which requires care or assistance on a regular basis to protect the claimant from hazards or dangers incident to his or her daily environment.

1.5.1.9. Not all of the disabling conditions in the list above are required to exist. It is only necessary that the evidence establish that the veteran or spouse needs “regular” (scheduled and ongoing) aid and attendance from someone else, not that there be a 24-hour need.

1.5.1.10. Determinations of a need for the Veterans Pension is based on medical reports and findings by private physicians or from hospital facilities. Authorization of Veterans Pension benefits is automatic if evidence establishes the claimant is a patient in a nursing home or that the claimant is blind or nearly blind or having severe visual problems.

1.5.2. Income Eligibility.

1.5.2.1. Under the current rules as of the date of this writing,² to be able to receive the Veterans Pension benefit, the veteran household cannot have adjusted income (*i.e.*, household income minus unreimbursed deductible medical expenses³) exceeding the Maximum Allowable Pension Rate-- MAPR -- for that veteran's Pension income category. If the adjusted income exceeds MAPR, there is no benefit. If adjusted income is less than the MAPR, the veteran receives a Pension income that is equal to the difference between MAPR and the household income adjusted for unreimbursed medical expenses. The Pension income is calculated based on 12 months of future household income, but paid monthly.

1.5.2.1.1. Proposed § 3.279(e)(8) will exclude from income annuities received under subchapter 1 of the Retired Serviceman's Family Protection Plan. 10 U.S.C. 1441.

² 38 U.S.C. § 1503(a)(8) authorizes VA, in determining annual income in the current pension program, to exclude from annual income amounts paid by a veteran, veteran's spouse, or surviving spouse, or by or on behalf of a veteran's child, for unreimbursed medical expenses to the extent they exceed 5 percent of the applicable maximum annual pension rate.

³ See section 1.5.5 for a discussion about what medical expenses are deductible under the new rules.

- 1.5.2.2. **Medical Costs and Long-Term Care Expenses:** a special provision for calculating Pension income allows household income to be reduced by 12 months worth of future, recurring medical expenses. Normally, income is only reduced by medical expenses incurred in the month of application. These allowable, annualized medical expenses are such things as health insurance premiums, home care expenses, the cost of paying a family member or other person to provide care, the cost of adult day care, the cost of an assisted living facility, or the cost of a nursing home.
- 1.5.2.3. This special provision is what allows veteran households earning more than the annual MAPR to qualify for the Veterans Pension Benefit. As an example, a veteran household earning \$6,000 a month could still qualify for the Veterans Pension Benefit if the veteran is paying \$4,500 to \$6,000 a month for nursing home costs. The applicant must submit appropriate evidence for a rating and for recurring costs in order to qualify for this special provision. VA typically does not tell applicants about this special treatment of medical expenses or how to qualify for it.

1.5.3. How is the Benefit Calculated?

- 1.5.3.1. The maximum annual pension rates are the annual pension rates set forth in 38 U.S.C. 1521 for veterans and 38 U.S.C. 1541 for surviving spouses. These maximum rates are then reduced by countable annual income, divided by 12, and rounded down to the nearest whole number to calculate the monthly pension entitlement rate. The maximum annual pension rate is the annual amount to which an eligible claimant is entitled to receive if his or her annual income is zero.
- 1.5.3.2. In other words, the monthly award is based on VA totaling 12 months of estimated future income and subtracting from that 12 months of estimated future, recurring and predictable medical expenses. Allowable medical expenses are reduced by a deductible to produce an adjusted medical expense which in turn is subtracted from the estimated 12 months of future income.
- 1.5.3.3. The new income derived from subtracting adjusted medical expenses from income is called “countable” income or IVAP (Income for Veterans Affairs Purposes). This countable income is then subtracted from the Maximum Allowable Pension Rate -- MAPR -- and that result is divided by 12 to determine the monthly income Pension award. This award is paid in addition to the family income that already exists.

1.5.4. Examples of Two Single Veterans in Assisted Living:

1.5.4.1. Both Veterans live in the same Assisted Living Facility and have the same retirement income. The only difference is that one pays \$20 more per month for his supplemental health insurance.

Veteran 1: First We Calculate Unreimbursed Monthly Medical Expenses

Assisted Living	\$3,500.00
Plus Medicare Part B	\$110.50
Plus Medicare Supplemental Medical Insurance	\$27.00
Equals Total Monthly Unreimbursed Medical Expenses	\$3,637.50
Minus 5% of Maximum Benefit (\$1,704)	\$85.20
Equals Countable Unreimbursed Monthly Medical Expenses	\$3,552.30

Veteran 1: Next We Calculate His IVAP

Total Monthly Income	\$3,572.30
Less Countable Unreimbursed Monthly Medical Expenses	\$3,552.30
Equals IVAP	\$20.00

Veteran 1: Lastly We Calculate His Aid & Attendance Pension Amount

Maximum Annual Pension Rate with Aid & Attendance	\$1,788.00
Less IVAP	\$20.00
Equals Total VA Pension Benefit per Month	\$1,768.00

Veteran 2: First We Calculate Unreimbursed Monthly Medical Expenses

Assisted Living	\$3,500.00
Medicare Part B	\$110.50
Medicare Supplemental Insurance	\$47.00
Total Unreimbursed Monthly Medical Expenses	\$3,657.50
Minus 5% of Maximum Benefit (\$1,704)	\$85.20

Equals Countable Unreimbursed Monthly Medical Expenses	\$3,572.30
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Veteran 2: Next We Calculate His IVAP

Total Monthly Income	\$3,572.30
Less Countable Unreimbursed Medical Expenses	\$3,572.30
Equals IVAP	\$0.00

Veteran 2: Lastly We Calculate His Aid & Attendance Pension Amount

Maximum Aid & Attendance Benefit	\$1,788.00
Less IVAP	\$0.00
Equals Total VA Pension Benefit per Month	\$1,788.00

1.5.5. Deductible Medical Expenses.

- 1.5.5.1. There is currently no regulation that adequately defines “medical expense” for VA purposes in order to determine which medical expenses are deductible from income in order to determine income eligibility. 38 USC § 1503(a)(8) authorizes VA, in determining annual income in the current pension program, to exclude from annual income amounts paid by a veteran, veteran's spouse, or surviving spouse, or by or on behalf of a veteran's child, for unreimbursed medical expenses to the extent they exceed 5 percent of the applicable maximum annual pension rate. The proposed regulation – § 3.278 – will improve clarity and consistency in determining what constitutes a medical expense that is deductible from a claimant's or beneficiary's income.
- 1.5.5.2. Proposed § 3.278 would implement 38 USC § 1315(f)(3) and 38 USC § 1503(a)(8) by describing and defining the medical expenses that VA may deduct for purposes of VA's needs-based pension programs. Proposed § 3.278(b)(1) would define “health care provider” as an individual licensed by a state or country to provide health care in the state or country in which the individual provides the health care. In paragraph (b)(1)(ii), the VA will include within the definition of “health care provider” a nursing assistant or home health aide who is supervised by a licensed health care provider.
- 1.5.5.3. Paragraphs (b)(2) and (b)(3) of proposed § 3.278 would define “activities of daily living” (ADL) and “instrumental activities of daily living” (IADL).

These terms are well-known and understood in the health care industry and are used in other Federal regulations, including VA regulations. For the purposes of determining deductible medical expenses for VA's needs-based benefits, ADLs would mean basic self-care activities and would consist of “bathing or showering, dressing, eating, toileting, and transferring.” We would also define “transferring” to mean an individual's moving himself or herself, such as getting in and out of bed. These activities are essentially those described in current § 3.352, and the inability to perform these activities is considered at least partly determinative of an individual's need for the regular aid and attendance of another individual for VA purposes.

- 1.5.5.4. Proposed § 3.278(b)(3) will define IADLs for VA medical expense deduction determinations as independent living activities, such as shopping, food preparation, housekeeping, laundering, managing finances, handling medications, using the telephone, and transportation for non-medical purposes. Proposed paragraph (e)(4) will provide that VA does not consider expenses for assistance with IADLs to be medical expenses except in certain circumstances because such personal care expenses are not intrinsically medical. The VA notes that other Government agencies, such as the Internal Revenue Service and Social Security Administration, also do not consider such expenses to be medical expenses for their purposes except in limited circumstances. One item that is often included as an IADL is transportation. The VA definition of IADL would include “transportation for non-medical purposes” because it is longstanding VA policy to consider transportation for medical purposes to be a deductible medical expense, and the VA will continue that policy.
- 1.5.5.5. Although managing finances is an IADL for purposes of this section, the VA will clarify that managing finances does not include services rendered by a VA-appointed fiduciary. The VA will also provide, in proposed paragraph (e)(5), that a fee paid to a VA-appointed fiduciary is not a deductible medical expense. Beneficiaries pay fees to VA-appointed fiduciaries out of their monthly VA benefits. Accordingly, the VA has determined that it would be inappropriate to permit a deduction from income for financial management services, and thus increase the amount of pension paid, when VA benefits are used to pay for the services.
- 1.5.5.6. Proposed § 3.278(b)(4) will define “custodial care” as regular assistance with two or more ADLs or regular supervision because an individual with a mental disorder is unsafe if left alone due to the mental disorder. This definition is consistent with current VA policy.
- 1.5.5.7. Proposed § 3.278(b)(5) will define “qualified relative.” Under 38 U.S.C. §§ 1503(a)(8) and 1315(f)(3), VA may deduct medical expenses paid by a

veteran, a veteran's dependent spouse, a surviving spouse. The implementing regulations, 38 CFR 3.262(l) and 3.272(g), limit whose medical expenses VA may deduct. In addition to the claimant's or beneficiary's medical expenses, the medical expenses of dependents and certain other family members are deductible. The VA will define "qualified relative" as a veteran's dependent spouse, a veteran's dependent or surviving child, and other relatives of the claimant who are members or constructive members of the claimant's household whose medical expenses are deductible under §§ 3.262(l) or 3.272(g). A "constructive member" of a household is an individual who would be a member of the household if the individual were not in a nursing home, away at school, or a similar situation. Defining a "qualified relative" for the purposes of the medical expense deduction makes the regulation simpler. The VA will not include veterans or surviving spouses in the definition because veterans and surviving spouses are the only pension beneficiaries who can be rated or presumed to require the aid and attendance of another individual or to be housebound under 38 CFR 3.351.

- 1.5.5.8. Proposed § 3.278(b)(6), the definition of "nursing home," would cross-reference current § 3.1(z)(1) or (2), which defines "nursing home" for all of 38 CFR part 3, with provision made that if the facility is not located in a state, then the facility must be licensed in the country in which it is located.
- 1.5.5.9. Consistent with current VA health care regulations, proposed paragraph (b)(7) will define "medical foster home" as a privately owned residence, recognized and approved by VA, that offers a non-institutional alternative to nursing home care for veterans who are unable to live alone safely due to chronic or terminal illness. See 38 CFR 17.73.
- 1.5.5.10. Proposed paragraph (b)(8) will define "assisted living, adult day care, or similar facility." The VA will use this lengthy term to avoid confusion that could result from the fact that not all facilities that meet the VA proposed definition use the same nomenclature. Some governmental institutions could also fall under the proposed definition. The proposed definition for such a facility is that it must provide individuals with custodial care; however, the facility may contract with a third-party provider to provide such care. The VA will further provide that residential facilities must be staffed with custodial care providers 24 hours a day, and must be licensed if such facilities are required to be licensed in the state or country in which the facility is located.
- 1.5.5.11. Proposed paragraph (c) would prescribe VA's general medical expense policy and list examples of expenses that VA considers medical

expenses for its needs-based benefits. In general, medical expenses for VA purposes are payments for items or services that are medically necessary or that improve a disabled individual's ability to function. This reflects longstanding VA policy with respect to medical expenses.

- 1.5.5.12. Proposed § 3.278(c) would specify that the term “medical expenses” includes, but is not limited to, payments specified in paragraphs (c)(1) through (c)(7). Paragraphs (c)(1) through (c)(7) list payments made to a health care provider; payments for medications, medical supplies, medical equipment, and medical food, vitamins, and supplements; payments for adaptive equipment; transportation expenses for medical purposes; health insurance premiums; smoking cessation products; and payments for institutional forms of care and in-home care as provided in paragraph (d). The VA will include in paragraph (c) detailed provisions relating to the broad categories of medical expenses. These clarifications will provide further guidance regarding the medical expenses that may be deducted from income.
- 1.5.5.13. Under current policy, medical expenses include payments for care provided by a health care provider, but not for cosmetic procedures that only improve or enhance appearance, although these may be deductible if the purpose of such procedure is to improve a congenital or accidental deformity or is related to treatment for a diagnosed medical condition. Proposed §§ 3.278(c)(1) and (e)(2) would continue this policy.
- 1.5.5.14. In § 3.278(c)(4), the VA will limit the deductible expense per mile for travel by private vehicle to the current Privately Owned Vehicle (POV) mileage reimbursement rate specified by the United States General Services Administration (GSA). The current amount can be obtained from www.gsa.gov, and will also be posted on VA's Web site at a location to be determined.
- 1.5.5.15. In proposed § 3.278(c)(5), the VA will clarify that medical expenses include Medicare Parts B and D premiums as well as long-term care insurance premiums.
- 1.5.5.16. Proposed § 3.278(d) will prescribe VA's medical expense policy for payments for institutional and in-home care services. In accordance with longstanding VA policy, proposed paragraph (d)(1) would provide that payments to hospitals, nursing homes, medical foster homes, and inpatient treatment centers, including the cost of meals and lodging charged by such facilities, are deductible medical expenses.

- 1.5.5.17. In paragraph (d)(2), the VA will clarify its policy with respect to in-home attendants, and limit the hourly in-home care rate that VA would deduct. The VA says this is to minimize instances of fraudulent or excessive in-home care charges. The VA will also require that payments, to qualify as medical expenses for VA, must be commensurate with the number of hours that the provider attends to the disabled individual. The proposed limit is reasonable and derived from a reputable industry source. The limit that we propose is the average hourly rate for home health aides, which is published annually by the MetLife Mature Market Institute in its “Market Survey of Long-Term Care Costs” (MetLife Survey).
- 1.5.5.18. The VA will next state the general rule that an in-home attendant must be a health care provider for the expense to qualify as a medical expense and that only payments for assistance with ADLs or health care services are medical expenses. **However, if a veteran or a surviving spouse meets the criteria for regular aid and attendance or is housebound, the attendant does not need to be a health care provider.** In addition, VA would consider payments for assistance with IADLs (as defined by VA) to be medical expenses, as long as the attendant's primary responsibility is to provide the veteran or surviving spouse health care services or custodial care. In accordance with current VA policy, this provision would also apply to a qualified relative if a physician or physician assistant states in writing that, due to physical or mental disability, the relative requires the health care services or custodial care that the in-home attendant provides.
- 1.5.5.19. Similarly, proposed paragraph (d)(3) will address facilities that are assisted living, adult day care, and similar facilities, and would provide the general rule that only payments for health care services and assistance with ADLs provided by a health care provider are medical expenses. **However, if a veteran or surviving spouse meets the criteria for regular aid and attendance or is housebound, the care does not need to be provided by a health care provider.** In addition, if the primary reason for the veteran or surviving spouse to be in the facility is to receive health care services or custodial care that the facility provides, then VA would deduct all fees paid to the facility, including meals and lodging. This provision would also apply to a qualified relative if a physician or physician assistant states in writing that, due to the relative's physical or mental disability, the relative requires the health care services or custodial care that the facility provides.
- 1.5.5.20. Proposed paragraph (e) will list examples of items and services that are not medical expenses for purposes of VA needs-based benefits. We

would clarify that generally, payments for items or services that benefit or maintain general health, such as vacations and dance classes, are not medical expenses, nor are fees paid to a VA-appointed fiduciary, as explained above. Proposed paragraph (e)(2) will provide that cosmetic procedures are not medical expenses except in the instances described in proposed paragraph (c)(1). We will also clarify that except as specifically provided, medical expenses do not include assistance with IADLs (i.e., shopping, food preparation, housekeeping, laundering, managing finances, handling medications, using the telephone, and transportation for non-medical purposes), nor do they include payments for meals and lodging, except in limited situations involving custodial care. Here, the VA will explicitly state that this category applies to facilities such as independent living facilities that do not provide individuals with health care services or custodial care.

- 1.5.5.21. VA's intent in promulgating these rules is to ensure that deductions from countable income reflect Congress' intent that amounts be deducted for "medical expenses" only, and not for other services such as meals and lodging or excessive administrative services not directly related to the provision of medical care.

1.5.6. Net Worth / Asset Test.

- 1.5.6.1. **The Old Asset Test.** There is an asset test to qualify for the Veterans Pension Benefit. Any asset or investment that could be easily converted into income might disqualify the claimant. Current regulations require the VA to deny or discontinue pension when, under all the circumstances, "it is reasonable" that the claimant or beneficiary use some portion of the applicable net worth for his or her maintenance. As of this writing, theoretically the maximum asset allowance for each applicant is based on an income and age analysis performed by the Department of Veteran Affairs. As of this writing, however, there is no specific dollar amount for the asset test and any amount of assets could block the award. Based on our experience and the experiences of other attorneys around the country, we recommend that clients reduce their countable assets to less than \$10,000 before applying for the Veterans Pension Benefit.

1.5.7. The New and Strange "Net Worth" Test.

- 1.5.7.1. Current 38 CFR §§ 3.274, 3.275, and 3.276 use the terms "net worth" and "corpus of the estate" to describe the assets available to a claimant or beneficiary that could bar pension entitlement if sufficiently great. In particular, current § 3.275(b) gives the same definition to both terms. The

new regulations will use the term “net worth” and it will be defined as the sum of a claimant's or beneficiary's assets and annual income.

1.5.7.1.1. The net worth limit for pension entitlement that the VA will be using is starting with the same as the standard maximum Community Spouse Resource Allowance (CSRA) prescribed by Congress for Medicaid, a similar Federal needs-based benefit program. For the Medicaid program, Congress has established a standard maximum resource amount that the “community spouse” of an institutionalized individual may be allowed to retain without the institutionalized spouse losing entitlement to Medicaid because of excessive resources. Congress established this standard maximum amount, referred to as the maximum CSRA, at \$60,000 in 1989 and indexed that amount for inflation by increasing it by the same percentage as the percentage increase in the average consumer price index for all urban consumers. See 42 U.S.C. 1396r-5(f) and (g).

1.5.7.1.2. For calendar-year 2016, the maximum CSRA is \$119,220, thus establishing a clear bright-line limit on net worth that an applicant for VA benefits can have. This is a good development in that Elder Law Attorneys can now plan for this benefit while knowing exactly how much a client can keep in the way of assets. The net worth limit would be the dollar amount of the current maximum CSRA as of the effective date of the final rule, to be increased regularly by the same percentage as the increase in Social Security benefits whenever there is a cost-of-living increase in benefit amounts payable under the Social Security Act. VA would publish the current limit on its Web site. It is interesting that they are not using the same CPI-based increase as is used by Medicaid.

1.5.7.1.3. Given that under the current rules, assets as low as \$10,000 can disqualify a veteran from receiving the pension benefit, this new net worth rule would at first seem quite generous. However, it's really not, as you will see in the next section.

1.5.8. Net Worth Calculation.

1.5.8.1. Proposed § 3.274(b)(1) will define a claimant's or beneficiary's **net worth as the sum of his or her assets and annual income**. The VA has proposed this new definition because under VA's net worth statutes, 38 U.S.C. 1522 and 1543, the VA says it “must consider a claimant's annual income when

determining if net worth bars pension entitlement.”⁴ To account for this statutory requirement, net worth for VA pension purposes would include both an asset component and an income component. This would be reflected for veterans and surviving spouses.

- 1.5.8.2. Proposed § 3.274(b)(2) would make it clear that “annual income” for net worth purposes is the same “annual income” used for calculating a pension entitlement rate for a claimant or a beneficiary. Note that the amount being used to calculate annual income is the full annual income BEFORE any deductions for unreimbursed medical expenses.
- 1.5.8.3. This definition of “net worth” defies all common sense as every 5th grader knows that “net worth” does not include income. Nevertheless, this is going to be the new rule that we have to live with.
- 1.5.8.4. Proposed § 3.274(c) will explain whose assets VA includes as a claimant's or beneficiary's assets. A veteran's assets include the assets of the veteran as well as the assets of the veteran's spouse, if the veteran has a spouse. See 38 U.S.C. 1522(a).
- 1.5.8.5. Nothing in current § 3.274 or any other current regulation prescribes when VA must calculate net worth for purposes of determining initial, continued, or increased pension entitlement. Accordingly, pursuant to new § 3.274(e), the VA will calculate net worth when VA receives: (1) An original pension claim, (2) a new pension claim after a period of non-entitlement, (3) a request to establish a new dependent, or (4) information that a veteran's, surviving spouse's, or child's net worth has increased or decreased.
- 1.5.8.6. Information about a claimant's net worth may come from the claimant him or herself or from VA matching programs with the Internal Revenue Service (IRS) or the Social Security Administration (SSA). Such matching programs are authorized under 38 U.S.C. 5317. VA would obtain information from the IRS and the SSA before paying pension and when re-calculating net worth for pension under § 3.274(e).

⁴ 38 U.S.C. §1522. **Net worth limitation.** States that (a) The Secretary shall deny or discontinue the payment of pension to a veteran under section 1513 or 1521 of this title when the corpus of the estate of the veteran or, if the veteran has a spouse, the corpus of the estates of the veteran and of the veteran's spouse is such that under all the circumstances, including consideration of the annual income of the veteran, the veteran's spouse, and the veteran's children, it is reasonable that some part of the corpus of such estates be consumed for the veteran's maintenance.

1.5.8.6.1. Nothing in current § 3.274 or any other VA regulation addresses the issue of whether claimants denied pension due to excessive net worth may lawfully decrease their net worth and qualify for pension. To remedy this omission, proposed § 3.274(f) will discuss the three ways in which claimants can decrease their net worth to lawfully qualify for pension. Under proposed § 3.274(f)(1), claimants could make certain expenditures to decrease their assets and thereby establish entitlement, continue entitlement, or increase entitlement to pension. Proposed § 3.274(f)(1) would limit authorized expenditures to expenditures for basic living expenses, education, or vocational rehabilitation. The VA claims that such limitations are consistent with the requirement in sections 1522 and 1543 that the individual consume some part of net worth for his or her maintenance when net worth is excessive. Given the purpose of the needs-based program established by Congress, the VA has interpreted “maintenance” to mean basic necessities such as food, clothing, shelter, or health care. Because education or vocational rehabilitation expenses can lead to decreased reliance on pension, the VA believes that such expenses should also be considered part of an individual's maintenance for this purpose.

1.5.8.6.2. A decrease in annual income is the second method by which net worth can decrease. In proposed § 3.274(f)(3), we the VA will address how it will treat payments, e.g., unreimbursed medical expenses, which can decrease either annual income or assets.

1.5.8.6.3. **VA would not consider the same payments to decrease both the annual income and the asset components of net worth.** Proposed § 3.274(f)(3) provides that VA will first apply the payment amounts to decrease annual income. The VA believes this is fair and reasonable because it is the amount of the annual income that determines the pension entitlement rate. If there are remaining deductible amounts (in other words, if medical expenses deductions reduce annual income to below zero) and net worth still exceeds the limit, VA will use those amounts to reduce the asset component of net worth.

1.5.9. Two Examples of Net Worth Calculation.

1.5.9.1. We start with the same basic facts: the net worth limit is \$119,220 and the maximum annual pension rate (MAPR) is \$21,466.

1.5.9.1.1. **Example 1.** A claimant has assets of \$115,000 and annual income of \$22,000. Adding annual income to assets produces a net

worth of \$137,000, which exceeds the net worth limit. The claimant pays unreimbursed medical expenses (UME) of \$17,780. VA first reduces the expenditures on UME from annual income, which decreases annual income to \$4,220. The claimant's net worth is now \$119,220 (\$115,000 +\$4,220); therefore, it is not necessary to apply the payment of UME to reduction of assets.

1.5.9.1.2. **Example 2.** A claimant has assets of \$125,000 and annual income of \$12,000. Adding annual income to assets produces a net worth of \$137,000 (same as the prior example), which exceeds the net worth limit. The claimant pays unreimbursed medical expenses (UME) of \$17,780. The VA first reduces the expenditures of UME from annual income, which decreases annual income from \$12,000 to \$0. That leaves \$5,780 of UME to be deducted from claimant's assets of \$125,000, leaving the claimant's assets (and net worth) at \$119,220.

1.5.9.2. Paragraphs (g), (h), and (i) of proposed § 3.274 are proposed net worth effective-date provisions. Proposed paragraph (g) is based on current § 3.660(d) and would prescribe the effective date of entitlement or increased entitlement after VA has denied, reduced, or discontinued a pension award based on excessive net worth. Proposed paragraph (g)(1) would describe the scope of the rule. Consistent with current § 3.660(d), proposed paragraph (g)(2) would prescribe the effective date of entitlement or increased entitlement as the day net worth ceases to exceed the limit as long as, before the pension claim has become finally adjudicated, the claimant or beneficiary submits a certified statement that net worth has decreased. "Finally adjudicated" is defined in 38 CFR 3.160(d), and for net worth decisions, means that the 1-year period for beginning the appeal process by filing a Notice of Disagreement (NOD) has expired or that the claim has been appealed and decided. If VA does not receive the certified statement within one year after VA's decision notice to the claimant of the denial, reduction, or discontinuance (and does not appeal), the effective date is the date VA receives a new pension claim. VA always has the right, under 38 CFR 3.277(a), to require that a claimant or beneficiary submit additional evidence to support entitlement or continuing entitlement as the situation warrants and proposed § 3.274(g)(2) would so provide.

1.5.10. Asset Exclusions.

1.5.10.1. For purpose of the for the Veterans Pension Benefit, the following assets are excluded from the net worth calculation:

1.5.10.1.1. Currently, the primary residence (even if the client is no longer living in it, but so long as it is not rented) is generally excluded from the asset test;

1.5.10.1.2. Proposed § 3.275 will provide that VA would not consider a claimant's primary residence, including a residential lot area not to exceed 2 acres, as an asset. Proposed § 3.275 would also provide that if the residence is sold, proceeds from the sale are assets unless the proceeds are used to purchase another residence within the calendar year of the sale;

1.5.10.1.3. **Outstanding mortgage loan not deductible.** VA will not subtract from a claimant's assets the amount of any mortgages or encumbrances on a claimant's primary residence.

1.5.10.1.4. **Claimant not residing in primary residence.** Although rental income counts as annual income as provided in § 3.271(d), VA will not include a claimant's primary residence as an asset even if the claimant resides in any of the following as defined in § 3.278(b):

1.5.10.1.4.1. A nursing home or medical foster home;

1.5.10.1.4.2. An assisted living or similar residential facility that provides custodial care; or

1.5.10.1.4.3. The home of a family member for custodial care.

1.5.10.1.5. However, it is important to remember that the home is not necessarily an exempt asset for purposes of Medicaid eligibility.

1.5.10.1.6. Value of personal effects suitable to and consistent with a reasonable mode of life, such as appliances and **family transportation vehicles**. However, it is important to remember that Medicaid only exempts one vehicle per family, not multiple vehicles.

1.6. Filing a Claim.

1.6.1. Complexity.

- 1.6.1.1. Filing a claim for the Veterans Pension Benefit is complex and time-consuming. If you want to do it correctly, it's important to get qualified assistance. Just knowing which form to fill out and how to complete it is a complex endeavor in itself. Even if the proper form is completed, failure to check a single box may result in a complete denial of your claim.
- 1.6.1.2. The application process involves: obtaining evidence of prospective, recurring medical expenses; evidence of medical need; appointments for VA powers of attorney and fiduciaries; and a thorough understanding of the application process. Often, qualification for this benefit involves reallocation of assets and shifting of income in order to qualify, and these reallocations may have significant impact on Medicaid eligibility.
- 1.6.1.3. Given that many veterans who need the Veterans Pension Benefit will most likely also need Medicaid in the future, this process should not be attempted without the help of an experienced Elder Law Attorney who thoroughly understands both the Veterans Pension Benefit and the Medicaid program, as well as the interaction between these two benefit programs.

SECTION 2. ASSET PROTECTION PLANNING UNDER THE NEW RULES

2.1. Half-Loaf Planning.

2.1.1. Basic Understanding.

- 2.1.1.1. The fact that the penalty period will apparently begin the first day of the month that follows the last asset transfer makes this new law similar to the old Medicaid gifting rules that were in effect prior to the Deficit Reduction Act of 2005 (“DRA”).
- 2.1.1.2. Under prior Medicaid law, someone already in a nursing home wanting to apply for Medicaid could give away half of his or her spend-down amount, immediately commencing the penalty period, and the nursing home resident would simply retain the other half to privately pay throughout the penalty period associated with the gift (as opposed to the Medicaid law since DRA, which says that the penalty period doesn’t start until someone has applied for Medicaid and is otherwise eligible “but for” the penalty period). This old Medicaid gifting strategy will now be available in connection with applications for the Veterans Pension. Below is an example of how this strategy works.

2.1.2. Half-Loaf Planning Example 1:

2.1.2.1. Let's assume that John Jones is a single veteran, so the maximum annual pension rate (MAPR) is \$21,466 (\$1,788 per month). The net worth limit is \$119,220. Mr. Jones has assets of \$200,000 and annual income of \$29,220 (\$2,435 per month) from Social Security. Adding his annual income to his assets produces a "net worth" of \$229,220, which exceeds the net worth limit by \$100,000, meaning that he has \$100,000 in assets to be protected. Let's further assume that he lives in an Assisted Living Facility and his monthly cost of care is \$6,000. Based on these assumptions, we can calculate his monthly shortfall as follows:

Assisted Living Facility Monthly Cost	\$6,000
Minus Monthly Income	\$2,435
Equals Monthly Assisted Living Shortfall	\$3,565

Now that we know his monthly shortfall, we can calculate how much of his assets can be transferred to the applicant's children and how much must be retained and spent on Assisted Living Expenses to cover his monthly shortfall during the penalty period.

\$3,565.00	Monthly Assisted Living Shortfall		Penalty & Payout Period ▼
\$100,000.00	Assets to be protected		
\$34,000.00	⇔ Amount to be Transferred to Children	Number of Resulting Penalty Months, rounded down ⇒	19
\$66,000.00	⇔ Amount to be Retained and Paid to ALF	Number of months that can be paid to ALF using the retained amount. ⇒	19

2.1.2.2. **Result:** After 19 months, \$34,000 out of the original \$100,000 has been protected and Mr. Jones can now apply for Aid and Attendance and begin receiving his VA pension amount of \$21,466 per year (\$1,788 per month).

2.1.3. Half-Loaf Planning Example 2:

2.1.3.1. Let's assume that Bill Smith is a married veteran, so the maximum annual pension rate (MAPR) is \$25,448 per year (\$2,120 per month). The net

worth limit is \$119,220. Mr. and Mrs. Smith have assets of \$230,000 and annual combined annual income of \$44,220 (\$3,685 per month) from Social Security. Adding their annual income to their assets produces a “net worth” of \$274,220, which exceeds their net worth limit by \$155,000, meaning that they have \$155,000 in assets to be protected. Let’s further assume that Mr. Smith lives in the memory unit of an Assisted Living Facility and his monthly cost of care is \$7,000. Based on these assumptions, we can calculate his monthly shortfall as follows:

Assisted Living Facility Monthly Cost	\$7,000
Minus Monthly Income	\$3,685
Equals Monthly Assisted Living Shortfall	\$3,315

Now that we know his monthly shortfall, we can calculate how much of his assets can be transferred to the their children and how much must be retained and spent on Bill’s Assisted Living Expenses to cover his monthly shortfall during the penalty period.

\$3,315	Monthly Assisted Living Shortfall		Penalty & Payout Period ▼
\$155,000	Assets to be protected		
\$60,500.00	⇔ Amount to be Transferred to Children	Number of Resulting Penalty Months, rounded down ⇒	29
\$94,500	⇔ Amount to be Retained and Paid to ALF	Number of months that can be paid to ALF using the retained amount. ⇒	29

2.1.3.2. **Result:** After 29 months, \$60,500 out of the original \$155,000 has been protected and Mr. Jones can now apply for Aid and Attendance and begin receiving his VA pension amount of \$25,448 per year (\$2,120 per month).

2.1.4. Practical Use of Half-Loaf Planning.

2.1.4.1. As a practical matter, many veterans who do not have high amounts of net worth should be able to use this half-loaf planning strategy as a means of protecting their assets. This strategy works so long as the Penalty & Payout

Period is less than 36 months using the above calculations. However, veterans with higher net worth should simply transfer their assets to a properly-drafted irrevocable asset protection trust and wait out the 3-year lookback period. This type of asset protection trust will be the topic of the remaining portion of this treatise.

2.2. Irrevocable Asset Protection Trusts for Veterans Pension and Medicaid.

2.2.1. Veterans of most states may create a Living Trust Plus™ Total Protection Trust to protect their assets.

2.2.1.1. For Veterans, the Living Trust Plus™ Total Protection Trust is the preferable form of asset protection trust because, for purposes of Veterans Special Pension eligibility, the Living Trust Plus™ is the **only** type of self-settled asset protection trust that allows a settlor to retain an interest in the trust while also protecting the assets from being counted by the Veterans Administration (and by state Medicaid agencies).

2.2.1.2. The settlor of the Living Trust Plus™ Total Protection Trust can serve as the Trustee,⁵ which is an important consideration for many persons wanting to establish an asset protection trust.

2.2.2. Practical Considerations.

2.2.2.1. Veterans seeking asset protection can not afford to ignore the potentially devastating costs of nursing home care and other long-term care.

2.2.2.2. Nursing homes are the most likely and one of the most expensive creditors that the average American is likely to face in his or her lifetime. Consider the following statistics:

2.2.2.2.1. About 70% of Americans who live to age 65 will need long-term care at some time in their lives,⁶ over 40 percent in a nursing home.⁷

⁵ See *supra* section 2.5.1, 2.5.2.

⁶ *Americans Fail to Act on Long Term Care Protection*, American Society on Aging, May 2003. National Clearinghouse for Long-Term Care Information, <http://www.longtermcare.gov> at http://www.longtermcare.gov/LTC/Main_Site/Understanding_Long_Term_Care/Basics/Basics.aspx#needs.

⁷ National Clearinghouse for Long-Term Care Information, <http://www.longtermcare.gov> at http://www.longtermcare.gov/LTC/Main_Site/Understanding_Long_Term_Care/Basics/Basics.aspx#needs.

2.2.2.2.2. As of 2008, the national average cost of a private room in a nursing home was \$212 per day or \$77,380 per year, and the national average cost of a semi-private room was \$191 per day or \$69,715 per year.⁸

2.2.2.2.3. On average, someone age 65 today will need some long-term care services for three years. Women need care for longer (on average 3.7 years) than do men (on average 2.2 years). While about one-third of today's 65-year-olds may never need long-term care services, 20 percent of them will need care for more than five years.⁹

2.2.2.2.4. Also, long-term care is not just needed by the elderly. A study by Unum, released in November, 2008, found that 46 percent of its group long-term care claimants were under the age of 65 at the time of disability.¹⁰

2.2.2.3. Contrast the above long-term care statistics with statistics for automobile accident claims and homeowner's insurance claims:

2.2.2.3.1. Between 2005 and 2007, an average of only 7.2% of people per year filed an automobile insurance claim.¹¹

2.2.2.3.2. Between 2002 and 2006, an average of only 6.15% of people per year filed a claim on their homeowner's insurance.¹²

2.3. Using Trusts for Aid and Attendance.

2.3.1. Reducing Countable Assets.

2.3.1.1. It has been and will remain a common planning practice for a veteran seeking to reduce net worth to transfer assets to a properly-drafted

⁸ The MetLife Market Survey of Nursing Home & Assisted Living Costs, October 2008.

⁹ National Clearinghouse for Long-Term Care Information, <http://www.longtermcare.gov> at http://www.longtermcare.gov/LTC/Main_Site/Understanding_Long_Term_Care/Basics/Basics.aspx#needs.

¹⁰ Insurance Information Institute, <http://www.iii.org/media/facts/statsbyissue/longtermcare>.

¹¹ Insurance Institute for Highway Safety, <http://www.iii.org/media/facts/statsbyissue/auto>, based on data from the Highway Loss Data Institute.

¹² Insurance Institute for Highway Safety, <http://www.iii.org/media/facts/statsbyissue/homeowners>, based on data from the Insurance Services Office.

irrevocable trust in a sufficient amount to reduce the veteran's assets to an acceptable level before submitting an application for the Veteran's Aid and Attendance special pension benefit.

2.3.1.2. Not all irrevocable trusts, however, will allow the claimant to qualify for benefits. In fact, most irrevocable trusts, including income-only trusts that do work for Medicaid, do not work for Veteran's Asset Protection Planning.

2.3.1.3. Opinions from the VA counsel's offices make it clear that transfers of property to "special needs" trusts for the benefit of the veteran, particularly where the veteran is trustee, or other arrangements where the veteran retains any kind of "life estate" or "life interest" in the transferred property, will not result in the exclusion of the transferred property from the calculation of the veteran's net worth for purposes of the Aid and Attendance benefits.

2.3.1.4. As noted in a 1997 VA Office of General Counsel opinion¹³:

2.3.1.4.1. "[P]roperty and income from property may be countable as belonging to a claimant if the claimant possesses such control over the property that the claimant may direct that it be used for the claimant's benefit. Such control may be considered a sufficient ownership interest to bring the property within the scope of the pension laws. It follows that only property over which a claimant, or someone with legal authority to act on the claimant's behalf, has some control to use for the claimant's benefit can reasonably be expected to be consumed for a claimant's maintenance and thus be includable in the claimant's estate."

2.4. Tax Goals When Using Trusts for Aid and Attendance.

2.4.1. Keeping it a Grantor Trust.

2.4.1.1. The vast majority of Veterans who are attempting to get the Aid and Attendance benefit are Veterans who have estates that are not likely to be subject to Federal Estate Tax, so the goal in estate planning for these clients, just as with Medicaid Planning clients, is to create a trust that is a Grantor Trust for both income and Estate Tax purposes.

2.4.2. Grantor Trust for Income Tax Purposes.

¹³ VAOPGCPREC 33-97, 1997, page 4, citing VAOPGCPREC 15-92 (1992) and VAOPGCPREC 72-90 (1990).

2.4.2.1. An Irrevocable Trust can be made a “grantor trust” for income tax purposes by choosing one of the grantor trust powers that creates grantor trust status over income. The primary powers used for this purpose are:

2.4.2.1.1. **Right to receive income**¹⁴ – this power is used in the basic Living Trust Plus™ for Medicaid Asset Protection, but NOT in the Veterans Version of the Living Trust Plus™ Total Protection Trust;

2.4.2.1.2. **Right to substitute assets of equal value**¹⁵ – this power is NOT used in any Living Trust Plus™ as Medicaid and VA might construe this power as having “access” to principal;

2.4.2.1.3. **Right to change beneficiaries** (i.e., limited Power of Appointment) – this power is what is used in the Living Trust Plus™ basic version and Veterans version.

2.4.3. Estate Tax Inclusion.

2.4.3.1. All of these powers **also** provide Grantor Trust status over trust **principal**, so using these powers makes assets in the trust includable in the grantor's estate, which allows for the desired step-up in basis.

2.4.3.1.1. IRC Section 2036:

2.4.3.1.1.1. **Retained right to income.** says that “[t]he value of the gross estate shall include the value of all property to the extent of any interest therein of which the decedent has at any time made a transfer . . . under which he has retained for his life . . . the possession or enjoyment of, or the right to the income from, the property”

2.4.3.1.2. IRC Section 2038:

¹⁴ IRC § 674 (a): The grantor shall be treated as the owner of any portion of a trust in respect of which the beneficial enjoyment of the corpus **or the income therefrom** is subject to a power of disposition, exercisable by the grantor or a nonadverse party, or both, without the approval or consent of any adverse party. (emphasis added). Also IRC § 677 (a): The grantor shall be treated as the owner of any portion of a trust, whether or not he is treated as such owner under section 674, whose income without the approval or consent of any adverse party is, or, in the discretion of the grantor or a nonadverse party, or both, may be—
(1) distributed to the grantor or the grantor's spouse.

¹⁵ IRC 675(4)(C).

2.4.3.1.2.1. Power to alter by adding or changing beneficiaries;

2.4.3.1.2.2. Power to alter by distributing corpus without ascertainable standard.

2.4.3.2. However, we already know that the power to substitute assets of equal value can not be used in a Living Trust Plus™ because Medicaid and VA might construe this power as having “access” to principal.

2.4.3.3. Accordingly, the power to change beneficiaries is the only power that can safely be put into the Veteran's Trust that will achieve the desired goal of Estate Inclusion. For the reasons explained in Section 2.4.3.4, the power to change beneficiaries must be a lifetime power of appointment.

2.4.3.4. The settlor’s retained limited power of appointment over the trust corpus arguably must be a lifetime power of appointment and not just a testamentary power of appointment. IRS Memorandum 1208026 says that the retention of testamentary limited power of appointment is not in itself sufficient to make a gift incomplete. A “testamentary power does not (and cannot) affect the trust beneficiaries’ rights and interests in the property during the trust term. Rather, a trustee with complete discretion to distribute income and principal to the term beneficiaries may, in exercising his discretion, distribute some or all of the trust property during the trust term. The holder of a testamentary power has no authority to control or alter these distributions because his power relates only to the remainder, *i.e.*, the property that will still be in the trust when the beneficial term interests are terminated. *Citing* *Bowe-Parker*, Page on the Law of Wills § 45.12 (1962), *Bittker and Lokken*, *Federal Taxation of Income, Estate and Gifts* ¶ 226.6.7 (2011); *Howard M. Zaritsky*, *Tax Planning for Family Wealth Transfers* (4th ed. 2011 Cum. Supp. No. 2) ¶ 3.03[1].

2.4.3.5. In the case examined in IRS Memorandum 1208026, the Donor transferred property to the Trust and retained a testamentary limited power to appoint so much of it as would still be in the Trust at his or her death. The Donors did not retain any right to receive income or any right to affect the beneficial term interests of their children, other issue, and their spouses (and charities) during the Trust term. Accordingly, the IRS concluded that with respect to those interests, the Donors fully divested themselves of dominion and control of the property when they transferred the property to the Trust.

2.5. Trustee Considerations.

2.5.1. Can settlor Serve as Trustee for a Veterans Trust?

- 2.5.1.1. Although the settlor can absolutely act as trustee of the Living Trust Plus™ for Medicaid purposes, many attorneys believe that the settlor should not act as the trustee of a trust designed for Veterans Asset Protection.
- 2.5.1.2. The VA's warning is that “[p]roperty and income from property may be countable as belonging to a claimant if the claimant possesses such control over the property that the claimant may direct that it be used for the claimant's benefit.”
- 2.5.1.3. However, so long as the assets in the trust can not be used for the claimant's benefit, there should be no legal problem in having the claimant serve as trustee, unless the beneficiaries of the trust are residing in the Veteran's household, in which case the VA could attribute indirect benefit to the Veteran of distributions to the beneficiaries.
- 2.5.1.4. The ability of the claimant to serve as trustee is directly addressed by VAOPGCPREC 73-91, which presented the following two questions:
 - 2.5.1.4.1. “Would proceeds from a life-insurance policy received by a veteran and shares of stock inherited by a veteran, which are placed into a valid irrevocable trust for the benefit of the veteran's grandchildren with the veteran as trustee, be counted as income of the veteran for purposes of determining entitlement to improved-pension benefits?”
 - 2.5.1.4.2. “Would these assets be considered in determining the veteran's net worth for improved-pension purposes?”
- 2.5.1.5. In answering these questions, the VA Office of General Counsel stated as follows:
 - 2.5.1.5.1. “We consider that principle legally sound on the basis that, as explained by the Assistant General Counsel in Undigested Opinion, 2-5-63 (Veteran), only property over which the veteran has some control to use for the veteran's own benefit can reasonably be expected to be consumed for the veteran's maintenance per 38 U.S.C. § 1522.
 - 2.5.1.5.2. Under the circumstances described, the veteran in an individual capacity, as distinguished from a fiduciary capacity, would have no legal ownership of the property and no authority or right to use, control, or dispose of the property or the income therefrom for

the veteran's own benefit after the proposed transfer. Under these circumstances, subject to the following discussion, the trust assets would not be considered a part of the veteran's estate. Further, income derived by the trust from trust assets would not be counted as income of the veteran for pension purposes. See O.G.C. Prec. 72-90.

2.5.1.6. In answering these questions, the VA Office of General Counsel held as follows:

2.5.1.6.1. “Generally, where a veteran places assets into a valid irrevocable trust for the benefit of the veteran's grandchildren, with the veteran named as trustee, and where the veteran, in an individual capacity, has retained no right or interest in the property or the income therefrom and cannot exert control over these assets for the veteran's own benefit, the trust assets would not be counted in determining the veteran's net worth for improved-pension purposes, and trust income would not be considered income of the veteran.

2.5.1.6.2. “[However,] [i]f the beneficiaries of the trust are residing in the veteran's household and the veteran is receiving benefit from expenditures from the trust, a determination must be made under the facts of the particular case whether the veteran is exercising such control and use of the trust assets that the trust may be considered invalid for purposes of determining pension eligibility.”

2.5.2. Can settlor Can Remove or Replace Trustee.

2.5.2.1. The same logic applies as above.

SECTION 3. PRACTICE TOOLS.

3.1. Evan Farr’s Living Trust Plus™ Asset Protection System.

3.1.1. <http://www.LivingTrustPlus.com>