1991

Planning for Medicaid Qualification

Louis A. Mezzullo

PLANNING FOR MEDICAID QUALIFICATION

By

Louis A. Mezzullo
Mezzullo & McCandlish
Richmond, Virginia

(September 17, 1991)

A. In General.

1. Medicaid is a federal-state program providing medical assistance to certain categories of the poor.

   a. Medicaid was enacted in 1965 as a companion to Medicare.

   b. Medicaid does not reimburse the covered person but pays the provider directly.

   c. Medicaid is administered by the Federal Health Care Financing Administration (HCFA) of the Department of Health and Human Services and by the applicable state agencies.

   d. Many of the regulations governing the Medicaid program are promulgated at the state level and can differ considerably from one state to another. One should check state regulations closely before advising clients.

2. In general, Medicaid covers persons 65 and over, disabled persons, and blind persons who satisfy certain income and resource requirements. 42 U.S.C. § 1396.

   a. Individuals generally must have monthly income less than the benefit rate provided under the Supplemental Security Income program, currently $407 per month, although this amount may vary depending upon the state and the amount of the person's resources. 42 CFR § 435.831(b).

   b. Generally, a person's resources cannot exceed $2,000 ($3,000 for a couple), but this is also subject to the person's monthly income and the state in which the person lives.

3. In general, the following benefits are provided under Medicaid:

   a. Medicare Part B premiums, deductibles and coinsurance;

   b. Inpatient hospital services with limitations and deductibles;

   c. Outpatient hospital and rural health clinic services;

   d. Nursing home care;

   e. Physician services;

   f. Transportation;

   g. X-ray and laboratory services;

   h. Home health care services;

   i. Clinic services, subject to a copayment in some cases;

   j. Prescription drugs, also subject to a copayment;

   k. Preauthorized medical supplies and equipment in limited circumstances;

   l. Physical therapy and related services; and

   m. Emergency hospital services.

   42 U.S.C. § 1396d(a).

B. Resource Limitations.

1. In determining the resources available to a person for purposes of qualifying for Medicaid treatment, the following resources are not counted:

   a. The home (subject to certain limitations discussed in the next paragraph);

   b. Household furnishings, such as furniture, paintings, appliances and electronics, which are exempt only while being used in the applicant's home;

c. Personal effects, including clothing, jewelry, photographs, etc.;

d. One automobile;

e. Property essential to the institutionalized person's self-support;

(1) In Virginia, up to $6,000 in income producing property, as long as the return on equity is equal to six percent or more. Virginia Medicaid Manual, Vol. XIII, Part II, Chap. C at 10.

f. Permanent life insurance, but only up to $1,500 of face value, and all life insurance with no cash value (term insurance);

g. Burial funds, up to $2,500 in Virginia (reduced by the face value of any cash value life insurance policies otherwise exempted and any amounts held in an irrevocable burial fund trust); and

h. Cemetery plots.

42 U.S.C. § 1382b.

i. In Virginia, life estates in real property are also excluded. Virginia Medicaid Manual, Vol. XIII, Part II, Chap. D at 4.

2. The home will be treated as a resource after the owner has been institutionalized for six months unless a spouse or a minor, blind, or disabled child continues to reside in the home or it can be shown that the patient will be able to leave the institution and return home.

a. The state may impose a lien on the home of a Medicaid patient to recover the cost of nursing home care when either:

(1) The patient cannot reasonably be expected to return home and the home is not occupied by the patient's spouse or a minor, blind or disabled child; or

(2) The patient dies.

42 U.S.C. § 1396p(a).

3. In determining available resources, the following rules are applied:

   a. Joint accounts are not considered a resource of the recipient to the extent it can be substantiated that the funds in the account belong to the other tenant and the account was established for the convenience of the other tenant.

      (1) Otherwise, a pro rata share will be considered available to the recipient.

      (2) One-half of a joint account will be treated as belonging to each spouse when the couple separates because of the institutionalization of one of the spouses. 42 U.S.C. § 1396r-5(b)(2)(A)(ii).

   b. An interest in an undivided estate is treated as an available resource unless the interest is unsalable for reasons other than being an interest in an undivided estate.

   c. The assets of a trust will be treated as a resource of the beneficiary to the extent the beneficiary can withdraw the assets. 42 U.S.C. § 1396a(k).

   d. If a trust was established by a grantor during his or her lifetime, the income and principal of the trust will be treated as available to the grantor or the grantor's spouse to the extent the trustee may pay out the income or principal to the grantor or the grantor's spouse, regardless of the purpose in establishing the trust, the revocability of the trust, or the use of discretion by the trustee. 42 U.S.C. § 1396a(k).

      (1) Such a trust is referred to as a Medicaid qualifying trust.

      (2) Although a testamentary trust will not be treated as a Medicaid qualifying trust, any income or principal that is required to be paid to a beneficiary will be included for purposes of determining whether the beneficiary satisfies the income or resource limit.

4. Transfers of property.

a. For purposes of determining the eligibility of a person for nursing facility services only, a transfer of assets by either spouse for less than fair market value will deprive the person of Medicaid eligibility for a period of up to 30 months.

(1) The number of months of ineligibility is determined by dividing the fair market value of the property transferred by the state's average private pay nursing home monthly charge (currently $2,230 in Virginia).

(a) For example, if the average private pay nursing home monthly charge is $2,500, a transfer of an asset with a fair market value of $25,000 would deprive the transferor of eligibility for nursing home services for ten months.

(2) The total number of months cannot exceed 30 regardless of the value of the property transferred.

42 U.S.C. § 1396p(c)(1).

(3) Under Virginia Code § 20-88.01, a transferee of assets may be required to reimburse the state for expenses paid if the transfer occurred within four years of the date the transferor is determined eligible for Medicaid and the uncompensated value of the transfer is at least $8,000. This provision may conflict with federal law.

b. A transfer between an institutionalized spouse (the spouse who is receiving care in a nursing home) and a community spouse (the spouse who remains in the home) is protected if the community spouse does not transfer the resources to another person for less than fair market value.

(1) In addition, transfers to a minor, blind or disabled child are protected.

42 U.S.C. § 1396p(c)(2).

c. A transfer of a home is permitted to:

(1) The person's spouse;

(a) Some commentators have stated that the law is not entirely clear on whether the transfer of the home to a spouse is protected only if the spouse does not retransfer the home to a third party. See Longenecker, "Financial and Health Care Planning for the Elderly: Alternatives for Financial Management, Federal Aid Eligibility and Termination of Medical Care," 16th Annual Notre Dame Tax and Estate Planning Institute, pp. 2-47 through 2-49 (1990).

(2) The person's child if the child is a minor, or blind or disabled;

(3) The person's brother or sister who already has an equity interest in the home and who has resided in the home for at least one year before the institutionalization of the person; and

(4) The person's child who is not a minor, or blind or disabled, but who has resided in the person's home for at least two years before the person's institutionalization and who provided care that enabled the person to reside at home rather than in a nursing home.

42 U.S.C. § 1396p(c)(2)(A).

d. A transfer of an asset will not affect eligibility if the person can demonstrate through objective evidence that:

(1) He or she intended to receive fair market value or other valuable consideration;

(2) He or she disposed of the asset exclusively for a purpose other than Medicaid eligibility; or

(3) Denial of eligibility "would work an undue hardship."

42 U.S.C. §§ 1396p(c)(2)(C) and (D).

C. Spousal Impoverishment.

1. In determining the income of a married person, the income of both the institutionalized spouse and the community spouse must be considered.

a. Since September 30, 1989, the income of the community spouse is not treated as available to the institutionalized spouse, except pursuant to a support order under a state's domestic relations law. 42 U.S.C. § 1396r-5(b)(1).

b. Also since September 30, 1989, the income of the institutionalized spouse is available to the community spouse to the extent that it is necessary to bring the income of the community spouse up to the minimum monthly maintenance needs allowance, which is an amount that equals the sum of a basic spousal allowance plus a housing allowance.

(1) The basic spousal allowance is currently 133 percent of the poverty level for a family of two.

(a) On July 1, 1992, the basic spousal allowance increases to 150 percent of the poverty level for a family of two.

(b) The basic spousal allowance is capped at an inflation-indexed amount of $1,500 ($1,662 in 1991).

(2) The housing allowance is the excess of the spouse's housing costs (rent, principal, interest, taxes, insurance, condominium fees, and a utility allowance ($137 per month for a household of one to three members, $172 for more than three)) over 30 percent of

the basic spousal allowance determined in paragraph (1) above.

42 U.S.C. §§ 1396r-5(d)(3) and (4).

c. The community spouse's income allowance may be increased by either:

(1) Court ordered spousal support; or

(2) A fair hearing if the spouse can demonstrate that exceptional circumstances exist which result in significant financial duress.

42 U.S.C. §§ 1396r-5(d)(5) and (e).

d. The income of the institutionalized spouse also may be used for maintaining other family members living with the community spouse.

(1) The amount is equal to one-third of the difference between the family member's gross income and the basic spousal allowance.

42 U.S.C. § 1396r-5(d)(1)(C).

2. Since September 30, 1989, the resources of both the husband and wife are considered together in determining whether the institutionalized spouse satisfies the resource limitation.

a. The community spouse is permitted to retain the greater of $12,000 or one-half of the value of the total nonexempt resources of the couple, but not in excess of $60,000.

(1) The $12,000 amount may be increased by state law up to $60,000.

(2) Both amounts are adjusted for cost-of-living increases.

(3) The amounts for 1991 are $13,296 and $66,480.

42 U.S.C. § 1396r-5(f)(2).

b. Either spouse may seek an assessment of the value of the nonexempt resources at the time

a spouse is institutionalized (referred to as the "snapshot"), and this amount will apply when the institutionalized spouse applies for Medicaid to determine the resources that may be retained by the community spouse. 42 U.S.C. § 1396r-5(c)(1)(B).

c. In addition, the community spouse's share of resources can be increased pursuant to a fair hearing. 42 U.S.C. § 1396r-5(e)(2).

(1) The increase may be needed to raise the income of the community spouse to the minimum monthly maintenance needs allowance.

D. Planning.

1. General observations.

a. If a person has sufficient resources to produce enough income to pay for long-term care, the person does not need to consider either the purchase of long-term care insurance or eligibility for Medicaid.

b. Likewise, if the resources of a married couple are sufficient to pay for the long-term care of both spouses, it will not be necessary to purchase long-term care insurance or to consider eligibility for Medicaid.

c. If the resources available to a single person or a married couple are not sufficient to pay for institutionalization, then the purchase of long-term care insurance or eligibility for Medicaid is important for two reasons:

(1) To protect assets for the community spouse in the case of a married couple; and

(2) To preserve assets for children and other beneficiaries.

d. It should be recognized that neither Medicare nor Medigap insurance will pay for long-term care.

(1) Medicare will pay for nursing facility charges only:

(a) If the patient is in a certified Medicare skilled nursing facility;

(b) If the patient's stay in the nursing facility follows an inpatient hospital stay; and

(c) For only a period of up to 100 days per spell of illness.

(2) Medigap policies (supplemental policies to Medicare coverage) cover a portion of the medical expenses not covered by Medicare, i.e., the deductible and copayment amounts.

(a) Typically Medigap policies do not cover long-term care; however, some Medigap policies do.

e. It should be recognized that most people will have at least some income from Social Security or other sources to pay part of the nursing home costs, even after the person becomes eligible for Medicaid.

(1) The institutionalized spouse may keep between $30 to $70 of his or her income for personal needs ($30 in Virginia).

(2) If the institutionalized spouse has no income or income below the personal needs allowance, the difference will be paid by the state.

(3) In most states, including Virginia, even though a person's income exceeds the limit for Medicaid eligibility for a noninstitutionalized person, the state will still pay the difference between the person's income and the nursing home charge, plus allow the person a monthly allowance of between $30 and $70 ($30 in Virginia), once the person's nonexempt resources have been spent down to $2,000.

(4) In those states that do not pay the difference, a person whose income

exceeds the Medicaid eligibility limit but is less than the cost of nursing home care will be forced to either remain out of a nursing home or rely on other persons to supplement the difference.

(5) In some states that do not pay the difference, such as Colorado, it has become the practice for a guardian of an incompetent institutionalized person to establish a trust that becomes legally entitled to receive all the person's income.

(a) The terms of the trust direct that income slightly less than the Medicaid limit is to be paid for the nursing home care of the person.

(b) The excess income in the trust can be used for the supplemental needs of the institutionalized person.

(c) At the death of the institutionalized person any balance in the trust will be paid to the state's Medicaid system.

f. Transferring assets to qualify for Medicaid is not immoral, unethical, or fraudulent.

(1) Today the middle class, for the most part, views Medicaid as an entitlement to preserve assets for the support of the community spouse or to provide inheritance for children.

(2) Planning for Medicaid eligibility is analogous to estate planning.

(a) An estate planner advises his or her client to transfer assets during lifetime, particularly using the annual exclusion, to reduce the person's gross estate for federal estate tax purposes.

(b) A person advising someone to transfer assets to qualify for Medicaid is reducing the person's

estate so that the government will pay for nursing home care.

(c) In both instances, the transfer of assets is resulting in additional revenue loss to the government.

(3) However, there are a number of reasons why a person may not want to deplete his or her resources to qualify for Medicaid:

(a) The person must become impoverished, which may be psychologically and socially traumatic, particularly for a person brought up with traditional middle class values.

(b) Even though illegal, there is perceived discrimination in nursing homes with respect to the treatment of Medicaid patients.

(c) The services available to a person on Medicaid are limited.

(d) It may be difficult to locate a bed in a nursing home if the person will enter the nursing home as a Medicaid patient, even though again, this is an illegal practice.

(e) If the person becomes hospitalized, the state may not pay to have the person's nursing home bed held until the person is discharged from the hospital, thereby forcing the person to return to a different room and perhaps even a different nursing home.

i) Virginia has recently eliminated any Medicaid payments to hold a Medicaid patient's bed during hospitalization.

ii) Familiar surroundings are extremely important to the

psychological and social well-being of an elderly person.

(f) The person's ability to care for himself or herself may improve to the extent the person no longer requires nursing care. However, when the person returns to the community, the person will be a pauper.

g. Ethical considerations.

(1) The advisor should determine who is the client, i.e., the senior citizen or the senior citizen's family.

(a) In many cases it will be a child or other relative of the senior citizen who first comes to the advisor.

(2) At that point, the lawyer needs to make it clear that he or she will represent either the family members or the senior citizen, unless it is appropriate to represent the entire family and all consent.

(a) The lawyer can represent both the senior citizen and other family members if it is obvious that he or she can represent each of their interests appropriately and they all consent to the multiple representation.

(3) If the lawyer will represent the senior citizen, but will be paid by the other family members, then ethical considerations require that the senior citizen consent to the payment arrangement.

(a) In addition, the lawyer must not allow the other family members to influence his or her professional judgment.

(4) If the lawyer represents the other family members, then he or she should

not give any legal advice to the senior citizen, but should advise the senior citizen to obtain separate counsel.

2. Lifetime Transfers.

   a. Perhaps the easiest way to protect assets from depletion due to institutionalization is to transfer the assets before the 30-month period.

      (1) Enough assets will need to be retained to pay for the period of institutionalization until the expiration of the 30-month period (or a shorter period if the fair market value of the transferred assets is less than 30 times the average private pay nursing home monthly charge).

      (2) If sufficient income or assets are not available, then the amount transferred may be required to be used to the extent necessary to pay for the care of the institutionalized person for the 30-month period.

      (3) For example, if the average monthly cost of nursing home care is $2,500, $75,000 ($2,500 times 30) would have to be spent on behalf of the institutionalized person before Medicaid would take over.

   b. Another technique involves transferring assets to the community spouse, followed by the refusal of the community spouse to spend down to the applicable resource limitation.

      (1) The state may be required to pay for the care of the institutionalized spouse under the hardship provision.

      (2) The state presumably could sue the community spouse, but in practice may not actually do so.

   c. One technique for transferring assets in anticipation of institutionalization involves the retention of assets with a fair market value equal to the fair market value of the assets transferred.

(1) For example, assume Mrs. Smith lives in a state where the current average private pay nursing home care monthly charge is $2,500. If Mrs. Smith, who has nonexempt assets worth $50,000, transfers an asset worth $25,000, she will not be eligible for Medicaid for ten months. Since she has retained $25,000 herself, she will be able to pay for her nursing home care for the ten-month period of ineligibility. Had she transferred the entire $50,000 at one time, she would have been ineligible for 20 months.

d. In the case of a wealthier person, multiple consecutive transfers may shorten the ineligibility period if the period of ineligibility resulting from each transfer runs concurrently rather than consecutively. It is unclear at this time whether this is the correct interpretation of the law.

(1) For example, assume that Mrs. Smith wants to transfer assets having a value of $137,500 and that the average monthly cost of nursing home care is $2,500. If Mrs. Smith transfers assets worth $25,000 at one time, her period of ineligibility as a result of the transfer is ten months ($25,000 divided by $2,500). If she transfers assets worth $22,500 the following month, her period of ineligibility as a result of the second transfer is nine months if the periods of ineligibility resulting from both transfers run concurrently, and 18 months if the periods of ineligibility resulting from both transfers run consecutively. If she reduces the amount transferred each subsequent month by the average monthly cost of nursing home care, her period ineligibility will not change, again assuming that the periods of ineligibility run concurrently.

(2) Since the benefit of using this technique is a period of ineligibility of less than 30 months, once the value of the amount to be given away exceeds

435 times the average monthly cost of nursing home care, there is no longer any benefit. The number 435 is derived by adding the numbers 1 through 29, since 29 is one less than 30, the maximum period of ineligibility regardless of the value of the assets transferred. The value of the assets in the first transfer would equal 29 times the average monthly cost of nursing home care, and each additional transfer would be reduced by the average monthly cost of nursing home care. The risk in using this technique is that after the last transfer is made, the remaining period of ineligibility may be determined as if the periods run consecutively rather than concurrently. However, in no event would the period of ineligibility after the last transfer extend for more than 30 months from the date of the last transfer.

e. Consideration should be given to transferring the home to the spouse before institutionalization, so that if it is desirable to sell the home later, this can be done by the community spouse after the determination of Medicaid eligibility has occurred, since assets received by the community spouse after the determination of eligibility of the institutionalized spouse should not be considered resources available for the expenses of the institutionalized spouse.

f. The home also may be transferred to:

(1) A minor child, or a disabled or blind child;

(2) A sibling who has an equity interest in the home and who has lived in the home for a period of one year before institutionalization; or

(3) A child who has lived in the home for a period of two years before institutionalization of the Medicaid recipient and who has enabled the recipient to remain in the home rather than to move to a nursing home.

g. Nonexempt assets can be used to purchase exempt assets or to pay down debts on exempt assets.

(1) For example, cash or other liquid assets could be used to prepay a mortgage on a home, or even used to purchase a new home.

(2) The use of funds to purchase exempt assets or to pay down obligations on exempt assets should occur after institutionalization but before the institutionalized spouse becomes eligible for Medicaid, so that the funds are taken out of the amount that must be spent down before eligibility rather than from the total amount that will be used to determine the share the community spouse may retain.

(a) For example, if the total amount of resources available to the husband and wife is $100,000, an equal division would result in $50,000 being allocated to the community spouse. Assuming that $10,000 is to be paid on a mortgage on an exempt home, if it is paid before the snapshot then the community spouse's amount is reduced to $45,000 (one-half of $90,000, the balance remaining after the mortgage payment), but if it is paid after the snapshot, then the community spouse's amount presumably stays at $50,000 (one-half of the $100,000 in total resources before the payment) and the amount of resources available to the institutionalized spouse would be reduced to $40,000.

(3) In order to increase the amount of nonexempt resources that the community spouse may retain, money could be borrowed using the exempt home as collateral, increasing the total resources of the couple. After the snapshot is taken, the mortgage can be paid down without reducing the amount

of resources that the community spouse may retain. This will not be beneficial once the value of the nonexempt resources exceeds twice the maximum amount of nonexempt resources that the community spouse is entitled to keep (currently $132,960, two times $66,480).

h. The community spouse could use resources to purchase an annuity. The annuity may not be considered a resource and the income would not be deemed available to the institutionalized spouse.

(1) The annuity should be nontransferable and not redeemable for cash.

(2) Any residual value (benefits paid to someone after the death of the annuitant) may be treated as a resource that has been transferred, resulting in a period of ineligibility for the annuitant and the annuitant's spouse.

i. Assets may be transferred to a Medicaid qualifying trust by either spouse and, to the extent that sufficient income and resources are retained to provide care for the institutionalized spouse during the 30-month period after the transfer, the assets in the trust will be protected from depletion, as long as the income or principal is not available to the institutionalized spouse and the principal is not available to the community spouse.

(1) The trust must be irrevocable.

(2) The income should not be required to be paid to the community spouse, so that if he or she does not need the income, the income will not accumulate in the hands of the community spouse, thereby becoming a resource that may delay his or her own eligibility for Medicaid.

(3) A special power of appointment may be granted to a child or other person to enable the holder of the power to distribute the principal to someone who may in turn use the principal for the

benefit of the grantor or to change the ultimate disposition of the assets remaining in the trust at the grantor's death.

(4) Consideration should be given to including a provision in a durable power of attorney authorizing the attorney-in-fact to transfer assets to other persons or an irrevocable trust to provide for the possible incompetency of a spouse who may become institutionalized.

3. Tax Consequences.

a. The donee will retain the same basis that the donor has in the transferred property for purposes of determining gain on a subsequent disposition, and will obtain a basis in the transferred property equal to its fair market value for purposes of determining loss.

(1) Consequently, the transferor can reduce his or her tax liability by selling the loss property and transferring the proceeds instead.

b. If the home is transferred, the $125,000 income tax exclusion available to a person age 55 and older will be lost.

(1) The exclusion may still be available if the transferee qualifies in his or her own right.

c. If the transferor retains the property until his or her death, the basis will be adjusted to the fair market value of the property at the date of death or the alternate valuation date if elected.

(1) Consequently, in a state like Virginia that does not treat a life estate as a resource, consideration should be given to having the transferor retain a life estate.

(a) As a result, the transferred property will be included in the transferor's estate for federal

estate tax purposes, giving the asset a step-up in basis for income tax purposes.

(b) The increase in estate taxes because of post-transfer appreciation may offset the income tax benefit.

d. Gift tax consequences should also be considered when transferring assets to qualify for Medicaid.

(1) To the extent that the value of the property transferred to a particular transferee in any year exceeds $10,000 (or $20,000 if the transferor is married and the couple elect to treat the gift as a split gift), the transfer will be treated as a taxable gift and will use up the transferor's unified credit.

(2) To the extent that the transferor has used up his or her unified credit, any additional transfers will be subject to gift tax.

4. Estate Planning Considerations.

a. The community spouse (or a spouse who expects the other spouse to be institutionalized) should consider not bequeathing assets to the other spouse.

(1) The surviving spouse's right to renounce the will under state law may be exercisable by the state.

(2) Assets could be placed in a trust with the surviving spouse as only a discretionary beneficiary, to avoid having the assets in the trust treated as a resource or the income of the trust treated as available to the surviving spouse.

(a) The community spouse should use a testamentary trust in this case to avoid having the trust treated as a Medicaid qualifying trust. Although a testamentary trust is

excluded from the definition of a Medicaid qualifying trust, there is no similar treatment for a revocable trust that becomes irrevocable at the death of a spouse.

b. Life insurance proceeds and retirement plan benefits, as well as any other assets passing outside the probate estate, should not be made payable to the institutionalized spouse or a spouse who is likely to be institutionalized.

(1) This may not be possible in the case of qualified retirement plan benefits if the nonparticipant spouse is not willing to sign a consent to the waiver, as required under the Equity Retirement Act of 1984.

(2) The state may treat a spouse's consent to the waiver as a transfer subject to the 30-month rule.

The institutionalized spouse may disclaim any assets passing to him or her; however, the disclaimer may either be disregarded for Medicaid qualification purposes or treated as a transfer subject to the 30-month ineligibility rule.