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Trusts and Estates A Practice Focus

New Rules, Tough Results

Sweeping Medicaid changes pose obstacles to nursing-home care.

By William S. Fralin

The Deficit Reduction Act of 2005 is the most significant change in federal Medicaid eligibility rules in 13 years.

The legislation aims to reduce Medicaid entitlement expenditures by $10 billion, as requested by President George W. Bush. It will make Medicaid eligibility far more difficult for millions of Americans, which is consistent with the administration's desire to create a society of personal responsibility.

These sweeping Medicaid changes, however, are likely to have unintended consequences. Gifts to family members and charities will be sharply curtailed, and nursing homes could face significant burdens in providing care to many residents ineligible for Medicaid and who have no remaining resources to pay for their care.

The act also will further complicate current complex federal and state statutes. Many who qualify for Medicaid will likely be denied coverage to which they are entitled. This will be either because of their inability to understand and complete the application process or because of their inability to provide the five years' worth of financial documentation required.

Most of the general public are unaware of the significant changes. In fact, many members of Congress who voted on this package are unaware of the provisions and the effects they will have on individuals, hospitals, and nursing homes.

Accordingly, lawyers ought to be aware of these changes and the consequences for clients (and for parents or other elderly relatives) if appropriate planning measures are not taken.

Five-Year Look Back

Among the major changes are:

• *The look-back period is extended from three to five years.*

Before the act, all individuals applying for Medicaid had to provide, in addition to the application, three years of financial documentation for the eligibility worker to review. The eligibility worker would then discern if any uncompensated transfers or gifts had been made in the preceding three years (36 months).

If gifts have been made, the government will impose an ineligibility period before the person qualifies for Medicaid. Because Medicaid was initially meant to be a welfare program for the truly underprivileged, the government wants to prevent people from transferring their wealth to family members and then immediately becoming eligible for assistance if the transferred funds could have been used to pay for care.

To prevent this, the government uses a delay calculation, based on the date and amount of the gift, that provides the corresponding period of ineligibility (i.e., the penalty period). The penalty calculation is made using the state's penalty divisor, which purportedly reflects the current average cost of care at a skilled nursing facility in that geographical region of the state.

Transfers where the donor receives goods or services of equivalent value to the amount of assets paid do not affect eligibility.

All applicants who apply for Medicaid after the effective date of the new legislation will be subject to up to five years (60 months) of financial review. Gifts within this time period can reduce Medicaid eligibility, but as with the previous look-back rules, any transfers *before* the five-year look back, regardless of the amount, would not affect eligibility.

Many applicants who may actually be eligible may not qualify if they cannot provide financial documentation for the five-year period. Many with declining health cannot produce or maintain the required financial documentation. It is also worth noting that all gifts—both to family members, including children and parents, and to charitable institutions—would be subject to these new rules.

• *The start date of the period of ineligibility is changed to the date a Medicaid application is filed.*

Under Medicaid rules a date is designated to calculate the period of ineligibility (penalty) resulting from transfers in the look-back period.

The prior law provided that the date of the penalty calculation

(that is, the day the penalty period begins) began on the first day of the month in which a transfer, either individual or serial, was made. The new law appears to set the start date for the penalty calculation at the date an applicant moves into a nursing home and files a Medicaid application.

A concern with this change in the start date of the penalty period is the financial hardship that both individuals and nursing homes will experience. The cost of providing care in nursing homes continues to climb faster than inflation. Increased federal mandates and regulatory requirements have placed tremendous stress on the nursing-home industry.

Approximately 60 percent of all nursing-home residents in the United States are Medicaid recipients. Nursing homes will have no means of being paid for their services by individuals who are ineligible because of this new rule. Yet federal law requires that nursing homes provide care for residents until they can be safely discharged, even if they cannot pay. Thus, because of the restriction on their ability to discharge residents, nursing homes attempt to prevent those who are unable to pay from arriving at their facility. And so if these individuals without Medicaid can't pay by other means, other facilities will not accept them.

For similar financial reasons, nursing homes will tend to dump indigent individuals at hospitals for needed or contrived medical services to get them out of their facilities, which will further stress an already overstrained hospital system.

And when these patients arrive at hospitals, the system Congress established that pays hospitals a set amount per medical treatment creates the incentive for hospitals to provide care as quickly as possible and then discharge the patients. But hospital workers already under significant pressure to place recovering patients in rehabilitation nursing homes will find they have no options if the individuals cannot pay for nursing-home services with Medicaid.

To illustrate the calculation of the current and former penalties, consider the following example:

Grandfather transfers $40,000 to a grandchild for college expenses. The monthly penalty divisor is $4,300. Under the prior rules the period of Medicaid ineligibility (penalty) would have begun immediately in the month of the gift, resulting in nine months of ineligibility ($40,000 ÷ $4,300 = 9.3). After that, Grandfather would be eligible to receive Medicaid payments.

Under the new rules, Grandfather will be eligible for Medicaid only after his funds are spent down to below $2,000, he has entered a nursing home, and he has filed a Medicaid application. And only then, when his assets are essentially gone, will the nine-month penalty period begin running, leaving Grandfather unable to pay for his care or qualify for eligibility.

Hardship Waivers

• *The effective date of the act is coming soon for most states.*

The act provides that the new transfer rules will affect all transactions occurring on or after the date of enactment, which officially occurred when the president signed the bill on Feb. 8. However, states have the option of implementing the rules at a later date if they require their own legislation to amend their state plans to bring them into compliance with the new law. In most states, the effective date probably will follow this year's legislative session.

• *Be aware of hardship waivers.*

To lessen the impact of the new rules, Congress is requiring every state to institute a hearing process to consider a hardship waiver for individuals. Such a waiver could be available when the period of ineligibility results in "a deprivation of medical care that would endanger the applicant's health or life or food or clothing or shelter or other necessities of life."

Nursing homes can apply for hardship upon the consent of the individual or that of the individual's legal representative. States have the option of paying the cost of care for up to 30 days while the application for a hardship waiver is pending.

• *The use of annuities is restricted.*

Concerns were raised about the use of annuities (which allow individuals to give away a lump sum of money to an insurance company and receive a stream of income payments in return) to evade eligibility restrictions. Thus, the use of annuities by Medicaid applicants and their families has been restricted. So-called balloon annuities, which pay a substantial final payment after a period of relatively small payments, are prohibited.

Any permitted annuities will have the new requirement that the state must be named the initial remainder beneficiary for at least the amount of the medical assistance paid on the beneficiary's behalf. This means that if the resident dies, any money left to be paid out by the insurance company must go first to the state to cover the medical bills. Whatever is left after that can go to the resident's heirs.

• *The income-first rule is now required.*

All states now must apply the so-called income-first rule. This is used to calculate an increase in the spouse's allowable resources above the permitted minimum monthly maintenance allowance to care for a spouse outside the nursing home. This allowance is the portion of the monthly income a spouse in an institution receives that may be kept by a spouse outside the nursing home to maintain his or her spouse in the community.

Under the old law some states permitted a resource-first rule, which let the request for an increase in income be met by allowing a community spouse to retain resources (as opposed to income) that would produce income sufficient to meet the expressed needs. Increased resources can be granted only to those who still have an income shortfall after receiving the income of the institutionalized spouse.

Home Equity

• *Home equity is no longer completely protected.*

Under the new enactment, if a nursing-home resident has home equity of more than $500,000, it will be considered an available resource to pay nursing-home bills. Previously, there was no limit to the amount of home equity one could protect in one's primary residence. If a spouse, a minor, or a disabled child lives in the home, the residence remains exempt regardless of value. States will have the option of exempting up to $750,000 in equity value at their discretion.

• *Refundable deposits for certain facilities will be considered available.*

The entrance deposits paid to continuing-care retirement com-

munities (which allow a resident to move from independent living to skilled nursing care) and life-care communities will be considered an available resource if the deposits can be refunded to an applicant, spouse, or other party.

Subject to the specific facility-entrance contract, such refunds occur when a resident moves from the facility or at his or her death. Formerly, the entrance deposit was considered to be the equivalent of owning a home (exempt resource), as many residents sold their previous home to make this payment, which was sometimes as high as several hundred thousand dollars. As such, the deposit was not considered an available resource to an applicant.

How the changes in the Deficit Reduction Act of 2005 will be implemented, interpreted, and applied are yet to be known. The enactment of enabling legislation and promulgation of rules by the states will significantly affect eligibility in each jurisdiction.

The Medicaid eligibility rules were complex and difficult to administer even before the new legislation. Given the added complexity and reporting requirements, the need for professional guidance and consultation will continue to grow.

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