Benevolent Benefactors Be Aware:

Changes in Medicaid Policy Result in Fairer Treatment of Gifts

By Laurie S. Frank and Jack K. Beckett

Making gifts is a double-edged sword for clients in need of long-term care. Estate and benefits planning attorneys have long recognized the advantages of gift-giving: For example, a plan that takes advantage of the $14,000 annual gift tax exclusion can help pare down an estate that would otherwise be subject to estate tax and can also preserve assets for a client who anticipates a lengthy nursing home stay. On the other hand, federal and state laws impose penalties on applicants for Medical Assistance Long-term Care (MALTC) benefits who have given away significant assets within five years of applying for benefits. Attorneys with clients who may be in need of long-term care should be aware of the significant changes to Maryland policy on these asset transfer penalties that came into effect on March 1, 2013. These changes make it more difficult for the Medical Assistance (Medicaid) program to penalize gifts that were made for purposes other than qualifying for MALTC benefits.

Manual Release 159 (MR-159), issued by the Maryland Department of Health and Mental Hygiene (DHMH), offers new guidance on transfers subject to penalty. For benefits planning attorneys, the most salient impact of MR-159 is it that it clarifies how the Medicaid program should determine whether an applicant or recipient (A/R) transferred assets for less than fair market value (FMV) for the purpose of qualifying for MALTC benefits. MR-159 provides new guidance in evaluating whether assets were given away to establish eligibility for benefits and explains what types of evidence may be submitted to prove the intent behind the transfer. This new policy is arguably more A/R-friendly, as it articulates a number of factual circumstances under which the Maryland MALTC program may not presume that assets were transferred for the purpose of qualifying for MALTC benefits. Additionally, MR-159 changes Maryland policy in several other areas, including agreements to make loans, the return of gifted funds, and undue hardship waiver requirements.

Law and Policy Before MR-159

Individuals in need of MALTC nursing home benefits or Home and Community-Based Waiver (HCBS) programs established under § 1915(c) of the Social Security Act have to contend with DHMH asset transfer penalty rules. Federal law states that, for a state Medicaid plan to receive federal cost-sharing, the plan must provide that an applicant, recipient, or spouse (A/R/S) will be ineligible to receive payment for nursing facility or HCBS services if the A/R/S disposes of assets for less than FMV within a specified "look-back period" (now, five years). The period of nonpayment is referred to as a "penalty period," and is equal to 1) the amount by which the FMV of the assets transferred during the look back exceeded the amount received in return divided by 2) the average monthly cost of private patient nursing facility services in the state. See 42 U.S.C. § 1396p(c)(1)(A)-(E). In Maryland, this penalty divisor is currently $6,800 (effective June 1, 2009). Maryland Medical Assistance Manual ("Manual"), Schedule MA-6. Following the Deficit Reduction Act (DRA) of 2005, the penalty period does not begin to run until the applicant is otherwise eligible to receive MALTC benefits—in other words, the individual must meet all eligibility requirements (technical, medical, resource, and income) before the penalty begins to run. 42 U.S.C. § 1396p(c)(1)(D)(ii). These rules generally discourage individuals from gifting assets to qualify for benefits and put those who gifted assets for other reasons at great risk of being denied benefits for needed long-term care.

However, federal law also states that if an individual can "make a satisfactory showing to the State [that] . . . (ii) the assets were transferred exclusively for a purpose other than to qualify for medical assistance," then the state should not assess a penalty for the transfer. 42 U.S.C. § 1396p(c)(2)(C)(ii). Maryland regulations state the same. Md. Code Regs. 10.09.24.08-1(B)(8)(f). In other words, the subjective intent behind a transfer matters, and only transfers made for the purpose of qualifying an individual for MALTC benefits may be penalized. Moreover, state plans have flexibility in determining which types of asset transfers they deem to have been made for this purpose.

Unfortunately, despite these "safe harbor" provisions, it was extremely difficult to demonstrate that an asset was transferred for a reason other than qualifying for MALTC benefits. This is because DHMH policy before MR-159 created a strong presumption that any asset transfer for less than FMV was made at least in part for the purpose of qualifying for MALTC benefits. See prior Manual, 800.23, p. 888 ("It is presumed that any disposal for less than FMV was made to establish or continue Medicaid eligibility or to avoid Medicaid's liens or recoveries provisions, unless the A/R successfully rebuts this presumption.")

Previous Maryland Medicaid policy listed several circumstances under which transfers for less than FMV may be permissible. See prior Manual, 800.23, p. 888. For example, transfers made before "the traumatic onset of disability" by an individual 60 years of age or younger, or small and regular donations to churches or charities, were not penalized. *Id*. However, regardless of whether the transfer fell within the permissible list, in practice it was difficult for applicants to establish that they had not transferred assets for the purpose of qualifying for benefits. Additionally, certain asset transfers were specifically identified as being subject to penalty where common sense would not suggest such an outcome—for example, payment of a grandchild's tuition. Prior Manual, 800.17(b), p. 864. In sum, pre-MR-159 policy created a presumption that all individuals aged 60 or over would require nursing home care in the future, and therefore anything that was given away was subject to penalty. See prior Manual, 800.23, p. 888. These rules created counterintuitive results in any number of factual circumstances. For example, under pre-MR-159 policy, an otherwise-healthy 62-year-old who paid for his daughter's wedding and suffered a debilitating stroke on the dance floor would

likely have been penalized for transferring assets for less than FMV.

Additionally, previous policy was not clear on how someone could prove that a transfer was made exclusively for purposes other than to qualify for MALTC benefits. The Manual simply stated that the A/R had the right to furnish "convincing documentary evidence" to the case manager. Prior Manual, 800.23, p. 888. Bank records, promissory notes, loan agreements, correspondence, contracts, and income tax forms were listed as acceptable forms of evidence. *Id*. Affidavits, one of the most useful tools for proving intent, were noticeably absent from this list.

In 2012, a group of attorneys from the MSBA Elder Law and Disability Rights section began working with state Senator Delores Kelley (Dem, District 10 - Baltimore County) to change DHMH's policy on transfers subject to penalty and to reconcile it with common sense notions of which types of transfers should be permitted. In March 2013, the policy changes were finalized, and in May 2013, DHMH issued MR-159, effective March 1, 2013.

MR-159

MR-159 accomplishes several related goals. First, it clarifies what types of proof may be furnished to establish that an asset was transferred exclusively for a purpose other than to qualify for MALTC benefits. Second, it sets forth a much more comprehensive list of circumstances that are sufficient to establish that an asset was transferred for purposes other than to qualify for MALTC benefits. MR-159 also contains several changes not directly related to rebutting the presumption that an asset was transferred to qualify for MALTC benefits, but which are worth discussing nonetheless.

a. Types Of Evidence

Existing policy was unclear as to what types of evidence could prove that an asset was transferred exclusively for reasons other than to qualify for MALTC benefits (although, as mentioned above, bank records, promissory notes, loan agreements, correspondence, contracts, and income tax forms were listed as acceptable forms of evidence). "[V]erbal assurances" were not "sufficient," and an individual had to provide "convincing evidence" to substantiate the reason for the transfer, as well as to show why there was no alternative to transferring the asset in question. Prior Manual, 800.20(d), p. 885.

MR-159 provides that "[w]ritten evidence must be presented to substantiate the specific purpose for which the asset was transferred such as bills, written agreements, oral agreements restated or ratified in written form at a later date, or affidavits." MR-159, p.27. It eliminates the "verbal assurances" language and the requirement that the evidence must show that there was no alternative to transferring the asset in question. *Id*.

Additionally, MR-159 articulates an expansive list of factual circumstances under which an asset transfer for less than FMV should not be penalized. Along with listing these circumstances, it provides the types of evidence that may be used to prove that such circumstances exist. This is discussed more fully in the next section.

b. New Circumstances

The previous policy articulated four specific circumstances that "could" constitute evidence that a transfer was made exclusively for purposes other than to qualify for Medical Assistance. In addition to the two mentioned above (small gifts to charities/churches, traumatic onset of disability in an under-60 individual), the unexpected loss of health insurance or of income or resources that would have provided payment for an individual's medical expenses were identified. Prior Manual, 800.23, p. 888.

MR-159 creates stronger protections for applicants and recipients. In addition to the four circumstances discussed above, under MR-159, "the presence of one or more of the following circumstances *shall* constitute evidence that the disposal was exclusively for a reason other than to qualify for Medicaid, and no penalty will be imposed:"

- The traumatic onset of a disability after the disposal (*e.g.*, accident, stroke, heart attack) (previous Manual editions limited this circumstance to individuals under age 60, but MR-159 eliminates the age requirement);
- Expenses related to traumatic onset of disability including payments made for family members' travel expenses (whether paid directly by the A/R/S or reimbursed to the family member(s)) to visit the A/R/S, including, but not limited to airfare, train fare, bus fare, gas, mileage reimbursement for wear and tear on automobiles, accommodations and food;
- A natural disaster affecting the A/R or a family member;
- Serious financial hardship of a family member, evidenced by an eviction notice, shut-off notice, foreclosure notice, repossession notice for business or farming equipment, or bankruptcy filing;
- Contribution to household

expenses, including, but not limited to, rent, mortgage utilities, cable, home maintenance, transportation and food, evidenced by written agreement or an oral agreement restated or ratified in written form at a later date;

- Charitable contributions up to $200 per donation per organization, or any amount if there is a consistent pattern of giving over several years, to an educational institution, religious institution, or other organization with a benevolent purpose and 501(c)(3) tax exemption status;
- Previous oral agreements (generally among family members) for compensation/payment for services reduced to writing at the time of application;
- Traditional gifts of up to $200 per person per event, or any amount if there is a consistent pattern of giving over several years, to family for weddings, holidays, religious milestones, graduation, birthdays and new births, and other special occasions;
- Payments to help family members or close friends or relatives pay for documented expenses for education;
- Payments to help family members or close friends or relatives pay for documented medical expenses; or
- Payments to modify a house for accessibility to enable the A/R/S to live there (including building an addition to the house), provided the A/R/S lives there for any period of time.

MR-159, pp. 31-32 (emphasis added).

This list covers a much broader range of factual circumstances than were covered under prior policy. Moreover, the use of the word "shall" indicates that it is mandatory for Medicaid to recognize the permissibility of asset transfers for less than FMV made under these circumstances. Finally, the list is meant to be illustrative and is not exhaustive; other circumstances may also be sufficient to establish that an asset was not transferred for the purpose of qualifying for MALTC benefits.

c. Other Changes

Most of the significant policy changes and clarifications in MR-159 relate to how an individual can demonstrate the intent behind an asset transfer. However, there are several other noteworthy developments in MR-159 not directly related to the intent issue.

Written and oral agreements may be restated and/or ratified: Under the DRA, a loan made by an A/R/S may be penalized as a disposal for less than FMV. This is the case unless the terms of the loan satisfy several requirements (*i.e.* unless the loan is "DRA-compliant"). To be DRA-compliant, the repayment terms of the loan must 1) be in writing, signed and dated by the lender and borrower; 2) be actuarially sound in accordance with Social Security life expectancy tables; 3) be legally binding; 4) prohibit cancellation of the remaining debt upon a lender's death; and 5) provide that payments to a lender shall be made in equal amounts during the loan's term with no deferral or balloon payments. Manual, 800.19, p. 873. MR-159 provides that oral agreements may be restated or ratified at a later date in written form. MR-159, p. 15. It also provides that "[i]f the A/R/S makes a loan that does not have all of these repayment terms, the loan is considered a disposal for less than FMV <u>unless</u> the loan is restated or ratified in a written agreement signed by both the A/R/S (or legal representative of A/R/S) and the borrower with all the repayment terms referenced above." MR-159, p.16 (emphasis added). In other words, an existing loan agreement that does not conform with the DRA requirements may be restated as a DRA-compliant loan.

Return of gifted funds: MR-159 also makes significant changes to DHMH's policy on what constitutes a return of gifted funds. Under Maryland's asset transfer penalty rules, when the recipient of gifted assets returns these funds to the A/R/S, this creates a corresponding reduction in the penalty period. Manual 800.24, p. 889. Benefits planning attorneys have long used the "gift and return" planning strategy to protect assets under this rule. Under gift and return, the A/R may gift assets to a trusted individual and apply for benefits to trigger eligibility and incur a penalty period. A portion of the assets may then be returned to the A/R to reduce the penalty period. The returned assets may be used to pay for the applicant's care while the reduced penalty period runs.

Under previous DHMH policy, the gifted assets had to actually be returned to the donor in order for the penalty period to be reduced. See prior Manual, 800.24, p. 890. Payment of the donor's cost of care by the gift recipient would not qualify as a return of funds. *Id*. MR-159 changes this rule, and "[i]f a payment is made for the A/R's bills or other expenses to the facility/company/provider by or on behalf of the person to whom the A/R/S transferred funds, the total amount of those payments is to be treated as a return in determining the amount that is transferred subject to penalty." MR-159, p 32. Although practitioners may still prefer to use the "clean" gift and return, this change

may offer some advantages. For example, the recipient of gifted assets may now be able to take advantage of the income tax deduction for payment of a dependent's medical expenses. See generally IRS Publication 502.

Undue hardship waiver: Finally, MR-159 relaxes some of DHMH's rules regarding undue hardship waivers. An individual subject to a penalty period may have the penalty waived if enforcement of the penalty would cause the individual undue hardship. Manual, 800.25, p. 891. Undue hardship exists if, because of imposition of the penalty, the individual would be placed at serious risk for deprivation of food, clothing, shelter, or other necessities of life, or medical risk such that his or her life would be endangered. *Id*. Under pre-MR-159 policy, the A/R was required to demonstrate that he or she had exhausted all legal remedies to recover the assets transferred, including pursuing an action in a court of law or equity. Prior Manual, 800.25, p. 892. Additionally, the A/R had to demonstrate that his or her age did not indicate a "predictable need" for long-term care services at the time the asset was transferred. *Id.* DHMH policy also presumed that undue hardship did not exist if the asset had been transferred to family members or relatives, and that these family members or relatives could make arrangements to return the assets or find other methods of financing the A/R's care, including accessing qualified retirement accounts. *Id.*

MR-159 removes these provisions. An A/R is no longer required to exhaust all of his or her legal remedies or prove that there was no predictable need for long-term care at the time of the asset transfer. MR-159, pp. 35-36. Furthermore, MR-159 eliminates the presumption that family members or relatives can make arrangements to pay for the A/R's care, and DHMH will no longer consider the gift recipient's qualified retirement accounts as being available to pay for care. *Id.*

Conclusion

MR-159 establishes a number of policy changes beneficial to Medicaid applicants, recipients, and their families. It makes DHMH policy more consistent with federal law, which prohibits transfer penalties from being imposed on transfers not made to qualify for Medical Assistance. It also brings the transfer penalties more closely in line with common-sense notions of what types of asset transfers constitute "gifts to establish Medicaid Eligibility" and therefore incur penalties. Finally, it offers much greater guidance to applicants on how they can prove the intent behind the asset transfers for less than FMV that they have made or plan on making. MR-159's full effect on benefits planning practice has yet to be seen, but it will likely lead to a greater emphasis on documenting and establishing this intent.

Ms. Frank is a partner at Frank, Frank & Scherr, LLC. She is a member of the MSBA Elder Law Section, the National Association of Social Workers, and the National Academy of Elder Law Attorneys. Mr. Beckett is an associate at Frank, Frank & Scherr, LLC, and a 2011 graduate of Washington and Lee University's School of Law.