NASMD

National Association of State Medicaid Directors

an affiliate of the American Public Human Services Association

March 10, 2010

Cynthia Mann
Director
Center for Medicaid and State Operations
7500 Security Blvd.
Baltimore, MD 21244

Re: Annuities

Dear Ms. Mann:

I am writing to you on behalf of the National Association of State Medicaid Directors (hereinafter "NASMD") as our member states are concerned and are increasingly being confronted with financial schemes that inappropriately shelter resources and assets from being properly counted under the Medicaid eligibility rules. In particular, in various states annuities are marketed, sold and made payable to the community spouse, however, these annuities were purchased with hundreds of thousands of dollars of the couple's resources. These annuities are marketed as "Medicaid compliant," meaning that the money used to purchase the annuity complies with the Deficit Reduction Act of 2005 (DRA) and cannot be sold on the secondary market, which would have rendered the market value of the annuity as a resource for eligibility purposes. This scheme has rendered three provisions of the Medicaid statute – the maximum Community Spouse Resource Allowance (CSRA); the "income first" rule; and the standard by which the CSRA can be raised – meaningless. For the reasons set forth below, we urge that you establish clear guidance, followed by regulations, to specify that these annuities are trust-like devices and the entire amount used to purchase these annuities must be counted in determining eligibility.

Time is of the essence in releasing guidance as there is a race by those marketing these annuities to have a controlling decision established in the judicial system. At this time the Third Circuit Court of Appeals, in an unpublished, non-precedential decision, has held that in these types of annuities, since the annuity payment is payable to the community spouse, it is income and should not be included in the eligibility calculations, regardless of whether it can be sold on the secondary market. Weatherbee v. Richman, 2009 U.S. App. LEXIS 24939 (2009). See also Vieth v. Ohio Dep't of Job & Family Servs., 2009 Ohio 3748 (Ohio Ct. App., Franklin County July 30, 2009), an unpublished case where a community spouse purchased an annuity with $140,000 and the court granted Medicaid benefits to the institutional spouse while permitting the community spouse to retain the annuity in addition to $101,630 as the CSRA. The New Jersey Superior Court, Appellate Division, however, reached the opposite conclusion and held that these annuities are countable for Medicaid purposes, because it could be sold in the secondary market. N.M. v. DMAHS 405 N.J. Super. 353 (2009). However, with these annuities becoming unmarketable by virtue of new endorsements, we fear it is a matter of time before a court will issue a controlling case that these annuities are a legitimate vehicle to shelter assets, which would make federal clarification at that point more difficult.

Congress has explicitly allowed annuities to be treated as trusts but only to the extent the Secretary specifies. 42 U.S.C. § 1396p(d)(6). We believe it is time the Secretary specifies that these annuities are trusts and that under the trust rules, the entire purchase price – which must be paid back to the community spouse to avoid a transfer penalty – is an available resource.

The common scenario is that after the institutionalized spouse enters the facility, the community spouse, usually with the help of an elder care attorney, liquidates the couple's resources and uses the funds to purchase a non-assignable, non-transferable annuity that meets all of the requirements under the Deficit Reduction Act of 2005. As such, there is no transfer penalty and, since the check is payable to the community spouse, the return of the resources is considered income to that spouse and is not used in the eligibility determination. As part of the package, the agent that assists in purchasing the annuity often provides three letters stating that the annuity cannot be sold on the secondary market. Thus, the couple has successfully retained the maximum set under the CSRA as well as any amount above the CSRA -whether $100,000 or $1,000,000 – that should be spent down on long term care prior to having taxpayers take over the bill.

These annuities make the statutory scheme that calculates the CSRA and sets a maximum CSRA irrelevant since there is no need to spend down after purchasing one of these annuities. There is also no concern that the community spouse won't have enough income as he or she is receiving monthly checks from the annuity for thousands of dollars.

These annuities are not the "legitimate retirement vehicles" that Congress sought to protect but merely launders otherwise countable resources into non-countable "income" of the community spouse. The majority of the monthly annuity check is not income under the Internal Revenue Code as it is return of principal with nominal interest attached. Since the DRA only requires the annuity pay out in the actuarially expected lifetime, these annuities often pay out quickly – 12 months or less – giving the community spouse several thousand dollars in "income" each month.

By using the resources to purchase an annuity that increases the community spouse's "income", the statutory rubric for protecting additional resources when the community spouse needs additional income is now a nullity. Congress has set forth explicit language that when the community spouse needs additional resources, the income of the institutionalized spouse must be considered first before additional resources are set aside. 42 U.S.C. § 1396r-5(d)(6) Like the maximum CSRA and specific requirements to raise it, the income first rule has no consequence or affect when a couple purchases one of these annuities. By placing all of the couple's assets into an annuity, the community spouse usually has monthly income of several thousand dollars so there is no need to transfer the institutionalized spouse's income to make up any shortfall. Why transfer income when the couple can protect literally any amount – even $1 million dollars – of resources?

One state has taken the position that a similar scheme - the promissory note - is a "trust-like" device. Like the annuities in question, these loans are conjured up solely to place assets out of the applicant's reach and to comply with the DRA section on promissory notes. The loan then pays out to the institutionalized individual while a penalty period for another outright gift (usually to the borrower) runs. A federal district judge has agreed that this state should be permitted discovery as to whether these notes are trust-like devices, rendering the entire "loan" amount a countable resource

At least a dozen states have expressed concerns about these "schemes" and we strongly urge you to follow the above state example and establish guidance to protect states from these financial schemes, which if permitted to continue, will lead to further diminishing state and federal resources to fund the Medicaid program.

Please do not hesitate to contact me if you have any questions or we can assist you in any way. I can be reached at 202-682-0100 x299 or akohler@aphsa.org. Thank you for your time and attention to this matter.

Sincerely,

Ann Clemency Kohler

Ann Clemency Kohler
NASMD Director

Cc: Barbara Edwards, CMSO DEHPG