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The Deficit Reduction Act of 2005 will have harsh impact on seniors, people with disabilities

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President Bush signed the Deficit Reduction Act of 2005 (DRA) on Feb. 8, 2006. The last major change to the Medicaid eligibility provisions of the federal Medicaid Act occurred in 1993 with the passage of the Omnibus Reconciliation Act of 1993 (known as OBRA '93). The DRA contains numerous provisions severely restricting Medicaid eligibility for the elderly and people with disabilities. This article will summarize the various changes wrought by the DRA and the impact of those changes on Medicaid eligibility. The following changes were enacted by the DRA:

• **1. Lookback Period** – The lookback period has been extended from 36 months to 60 months for all transfers (not just transfers to/from trusts). Under prior law, the lookback period was 36 months for outright transfers and 60 months only in the case of trust-related transfers. The lookback period refers to the period of time for which financial statements must be provided to the Medicaid agency. This includes accounts that were closed during such time period and all accounts that remained open at the time of application.

• **2. Commencement Date of Penalty Period** – Although it is presently unclear how this section of the law will be interpreted or applied, it is conceivable (see alternative interpretation below) that an ineligibility period resulting from an uncompensated transfer of assets during the 60-month look back period will not commence until the individual is residing in a nursing home, has assets below the resource allowance (this amount varies by state but cannot exceed $4,150 under federal law) and files a Medicaid application. Under prior law, the penalty period began on the first day of the month in which the transfer was made (or the following month, depending on the state). For example, under pre-DRA law, if the average cost of care for one month in a nursing home in the region where the Medicaid applicant lived was $5,000 per month, and the individual transferred $15,000, s/he would be ineligible for Medicaid for three months starting in the month in which the gift was made. Thus, if $15,000 was gifted in July 2005, and the individual entered a nursing home on Oct. 1, 2005, s/he would be eligible for Medicaid benefits because the three-month penalty period would have expired.

Under the DRA, the penalty period does not begin to run until the person is in a nursing home, has less than $4,150 (or the State resource allowance, if less) and submits a Medicaid application to trigger the running of the penalty period. Therefore, if an applicant gifted $15,000 on July 1, 2006 and went into a nursing home and applied for Medicaid on Oct. 1, 2006, s/he would not qualify. The penalty period does not begin to run until the individual is residing in the nursing home and has assets below the resource allowance. On Oct. 1, 2006, a three-month penalty period would first begin to run and the individual would not qualify for benefits until Jan. 1, 2007. Depending on the area in the country where the individual resides, the nursing home can cost anywhere from $5,000 to upwards of $12,000 per month. Having reduced his/her resources to less than $4,150, it is not clear how such an individual would be in a position to pay for the care needed from Oct. 1, 2006 - Dec. 31, 2006.

An alternative interpretation of the commencement date provisions is that the penalty period will begin to run when an individual applies for Medicaid and is receiving institutional level care, defined in the federal Medicaid Act as care provided in a nursing home, nursing home level care provided in any other facility or nursing home level care provided pursuant to a home and community-based waiver program. This would be a more sensible interpretation of the DRA; however, until the Center for Medicare and Medicaid Services issues a policy pronouncement on this issue, it remains unclear how these provisions will be applied.

The impact of the lookback period and commencement date of the penalty period provisions discussed above will be felt by many elderly and people with disabilities. It will have a chilling effect on charitable gifts and donations to political and religious organizations. Older family members will be inhibited from making commonly made family gifts to assist younger family members (i.e., for the purchase of a first home, college tuition, etc.). Medical providers will suffer financial harm as hospitals encounter difficulty arranging for admission into nursing facilities due to previously made gifts. Nursing homes will experience a suspension of payments due to persons already residing in nursing homes falling off the Medicaid roster. Some nursing homes may be forced to discharge residents or provide uncompensated care. Some individuals will not be aware of the need to file a Medicaid application just to begin the penalty period. There will be reduced access to needed care due to denials of admission into nursing homes. Informal caregivers will surrender jobs and relocate to provide care to the elderly, resulting in a huge societal and economic cost.

• **3. Home Equity Cap** – A home will not be permitted to have an equity value of greater than $500,000, unless a spouse, minor child under the age of 21, or blind or disabled child lives in the home. The $500,000 equity cap can be raised to up to $750,000 at the option of each state. For example, if an individual owns a home with an equity value of $530,000, and less than $4,150 in other assets, s/he will not qualify for Medicaid unless the equity value is reduced by $30,000. If an individual's home has an equity value which exceeds $500,000, s/he may reduce the equity value by taking a home equity loan or reverse mortgage, the proceeds of which would need to be spent on long term care needs before Medicaid benefits will commence.

The home equity cap applies to Medicaid applications filed on or after Jan. 1, 2006 (note that this date is different from the effective date for the rules regarding asset transfers, which applies to transfers made on or after Feb. 8, 2006). Under prior law, there was no cap on the amount of equity value that an individual could have in his/her home. Under pre-DRA law, one could transfer a home to a spouse, a disabled or blind child, a caretaker child (defined as a child who lived with a parent for at least two years prior to the parent's institutionalization which care delayed the parent's admission into a nursing facility), or a sibling with an equity interest in the home (defined as a sibling of the Medicaid applicant who owned equity in the home (not necessarily having his/her name on the deed but by virtue of contributing to the maintenance and upkeep of the home)). These exempt transfers remain available and were not affected by the DRA.

• **4. Annuities** – Under the DRA, in order for an annuity to be "DRA-compliant" and not count as a resource, the annuity must name the state as a remainder beneficiary. If, however, there is a spouse or a minor or disabled child, then that person may be named in the first position with the State being named as remainder beneficiary in the second position. Under prior law, annuities that were "actuarially sound" (defined as paying out in full over the life expectancy of the individual/annuitant and not over a longer period) were not considered resources of the individual for Medicaid eligibility purposes. In addition, certain states permitted the purchase of balloon annuities, which provided for a nominal principal payment each month along with an interest payment and a large "balloon" payment toward the end of the term of the annuity. The DRA prohibits the purchase of a balloon annuity for Medicaid eligibility purposes.

• **5. Life Estate** – The DRA permits an individual to purchase a life estate in a home owned by someone else (i.e., a family member) provided that s/he lives in the home for at least one year after the purchase of the life estate.

• **6. Fractional Penalty Periods Mandated** – Under pre-DRA law, a State was given the option to round down penalty periods. Thus, if an individual transferred $18,000 and the average cost of care was $5,000, the penalty period of 3.6 months would be rounded down to three months in a state that opted for rounding down the penalty period. The DRA prohibits rounding down by states.

• **7. Income First Rule Mandated** – Under pre-DRA law, states were given the option to apply either the resources first or the income-first approach to raising the Community Spouse Resource Allowance (known as the CSRA). Under the resources first approach, a state allowed a community spouse to keep assets above the CSRA (the federal maximum is currently $99,540) in order to generate additional income needed to meet the Minimum Monthly Maintenance Needs Allowance (currently up to $2,489 under federal law). If a community spouse had less than $2,489 of income, the question was whether she could keep assets above the $99,540 in order to generate the additional income needed to bring her up to $2,489 (this is known as the resources first approach) or must she accept a diversion of the institutionalized spouse's income first (this is known as the income-first approach), thereby requiring a spend-down of assets above the $99,540? The resources first approach was preferred since the community spouse often survived the death of the institutionalized spouse and desired to keep assets above the CSRA in order to continue living in the community after the institutionalized spouse died. Many states had opted to use the resources first approach prior to the enactment of the DRA. Under the DRA, all states must now use the less desirable income first approach.

• **8. Long Term Care Partnership Insurance Policies** – Under pre-DRA law, only four states were authorized to offer partnership plans, whereby an individual could purchase a stated amount of long-term care coverage (three years), qualify for Medicaid after the coverage period expired and keep all of his/her assets. The four states included California, Connecticut, Indiana, and New York. The individual's income still needed to be spent on the cost of the nursing home. The DRA extended the partnership program to all 50 states, so there will likely be a great deal of activity in this area.

• **9. Notes and Loans** – Under pre-DRA law, there was no statutory guidance as to how loans made by the Medicaid applicant would be treated. The DRA makes it clear that loans made by an individual applying for Medicaid must be actuarially sound (see annuity discussion above) in order for the loan not to be considered an available resource for Medicaid eligibility purposes.

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Furthermore, equal payments must be throughout the term of the loan and there can be no cancellation provision included in the note (this effectively eliminates self-cancelling installment notes whereby the entire principal balance of a note was eliminated upon the death of the Medicaid recipient).

• **10. Continuing Care Retirement Communities** – Under the DRA, continuing care retirement communities could force the spending of assets that were disclosed on an application for admission into the community before applying for Medicaid, and certain deposits would be countable toward Medicaid eligibility.

At this time, we in the elder law bar anticipate that the DRA will apply to transfers made on or after Feb. 8, 2006. While some states have already adopted rules and/or legislation implementing the DRA provisions at the state level, many other states have yet to do so. The non-implementing states are very likely awaiting issuance by the Center for Medicare & Medicaid Services of a policy pronouncement interpreting the various provisions of the DRA. That policy pronouncement has not yet been issued as of early July 2006, but is expected to be issued by September 2006. In those states that have yet to implement the DRA, the pre-DRA rules are being applied. The DRA changes should not affect a Medicaid application with transfers occurring solely between spouses as such transfers are exempt from the penalty period rules (this exemption remains unchanged by the DRA). Furthermore, there is a hardship exception that will permit certain Medicaid applicants to claim eligibility for Medicaid benefits notwithstanding ineligibility due to post-DRA rules if such denial would cause an undue hardship. This hardship exception was not particularly helpful under pre-DRA law and remains untested with regard to post-DRA Medicaid applications filed.

Clearly, the DRA will make it more difficult for seniors and people with disabilities to qualify for Medicaid benefits to pay for needed long-term care services. Perhaps the most significant lesson learned from the passage of the DRA is that it is even more important for people concerned about the costs of long-term care to plan ahead. Everyone should have an estate and long-term care plan in place which takes into account his/her goals and objectives for addressing long term care needs and asset preservation. The new DRA provisions are extremely complex and the landscape can now be described as a minefield littered with traps for the unwary. CSAs looking to work with an attorney well-versed in DRA-specific matters in their state canaccess the National Academy of Elder Law Attorneys' Web site at **www.naela.com.** ◆

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