

Recent Challenges to Medicaid Planning by Long Term Care Facilities

by

Andrew H. Hook, CELA and Thomas J. Begley Jr., CELA¹

The elderly population of the United States is rapidly growing, as is the demand for nursing home care. Nursing home care costs are also rising beyond the reach of most families. Many lower and middle-class families cannot afford to pay nursing home rates of \$5,000 to \$10,000 per month. Therefore, an increasing number of nursing home applicants have turned to elder law attorneys to pursue Medicaid planning, and obtain assistance with these high costs.

Nursing homes are generally not in favor of this Medicaid planning trend. In Virginia, a nursing home is reimbursed by Medicaid at an average of 75% (the “reimbursement rate”) of the private pay rate. Therefore, more Medicaid residents equal lower revenues for nursing homes. Not surprisingly, nursing homes have reacted to these developments, and have recently exhibited a determination to protect or collect their fees, including resorting to legal action, as illustrated by the following cases. This article will briefly discuss these cases, their potential impact, and implications for future Medicaid planning.

Oak Crest Village, Inc. v. Sherwood R. Murphy²

Maryland’s highest court, the Court of Appeals of Maryland, affirmed a trial court ruling that a continuing care retirement community’s Residence and Care Agreement provision was invalid as applied to a nursing home care resident, because the provision contravened state law by attempting to restrict the resident’s rights to seek Medicaid assistance.

Mr. Sherwood Murphy and his wife Ruth moved into Oak Crest Village, a Continuing Care Retirement Community (“CCRC”). Oak Crest provided three levels of care: independent living, assisted living, and nursing home care. Mr. Murphy entered the nursing home facility, while his wife entered an independent living apartment. Oak Crest’s payment structure required a substantial deposit, a commitment to pay future charges and the signing of a Residence and Care Agreement, which included a disclosure of the couple’s assets. Mr. and Mrs. Murphy owned over \$650,000 of assets, of which at least \$450,000 were jointly owned by Mr. and Mrs. Murphy when they entered the facility. On November 26, 2001, Mrs. Murphy signed two separate Residence and Care agreements, one for herself and one with an addendum, on behalf of her husband. Section 8.11 of those agreements provided in part,

¹This article will be reprinted in an upcoming issue of *Estate Planning*, published by RIA. The authors would like to thank Sandra Smith and Mark Pascucci, Elder Law attorneys, with the research for this article.

²Oak Crest Village, Inc. v. Mr. Sherwood R. Murphy, 379 Md. 229 (2004)

[to] protect Oak Crest from a situation wherein a Resident divests him/herself of those assets for the purpose of qualifying for assistance or reduction of Monthly Fees, Resident agrees not to divest him/herself of, sell, or transfer any assets or property interests (excluding expenditures for Resident's normal living expenses) that would result in a reduction in Resident's net worth (assets less liabilities) which is below the minimum criteria to become a Oak Crest resident, without having first obtained the written consent of Oak Crest.³

Section 8.11 also referred to Section 6.4 h. of the Agreement, which required a resident who was unable to pay for his care to take certain steps to obtain funds before applying for Medicaid. These steps included seeking assistance from family members and other means, including "county, state and federal aid or assistance, excluding Medicaid but including Medicare, public assistance and any other public benefit program." The addendum to the Agreement required the resident to seek Medicaid assistance if they were otherwise unable to pay for care. The addendum also provided that a resident was "not required to give up any of the Resident's rights to Medicaid benefits to be admitted or to stay at the Facility," and that Oak Crest would "accept Medicaid payments" if the resident was eligible. Mrs. Murphy had to sign the addendum, because it recited that she had access and management/control over her husband's income and assets.

Mrs. Murphy made transfers of assets that ultimately resulted in her husband's Medicaid eligibility. Shortly after entering the facility, Mrs. Murphy transferred \$356,000 to an account that was jointly titled with Mrs. Murphy and her daughter. Mrs. Murphy then used \$280,000 of the transferred funds to buy two annuities for herself. Mr. Murphy later applied for Medicaid and was found eligible as of June 1, 2002.

Upon learning of Mr. Murphy's Medicaid eligibility, Oak Crest filed suit for equitable and declaratory relief, alleging violation of the above provisions of the Residence Agreement, and sought to have Mrs. Murphy's \$356,000 transfer annulled. Alternatively, Oak Crest sought the right to rescind the contract because of the breach, terminate Mr. Murphy's membership, and discharge him from the nursing facility. The trial court ruled in favor of the Murphys.

The Court affirmed on appeal that Oak Crest could not enforce its contractual provisions against Mr. Murphy. The Court held that Oak Crest's nursing care wing was a Medicaid certified facility, as defined by state statute, because it participated in the Medicaid program. As a Medicaid certified facility, Oak Crest was required to follow Maryland Code HG § 19.345(b), which prohibited a Medicaid certified facility from requiring facility applicants to waive their rights to Medicaid or to agree to privately pay for their care for any period of time. Further, a certificate of registration, issued to Oak Crest by the Maryland Department of Aging, was not relevant to the question of whether § 19.345(b) was applicable to Oak Crest's Agreement.

³ Id.

Because § 19.345(b) applied to the nursing care wing of Oak Crest, the statute also applied to Mr. Murphy, because he entered and remained in Oak Crest's nursing care wing. As a result, the Court found that Section 8.11 of Oak Crest's Residence and Care Agreement, which attempted to restrict Mr. Murphy's Medicaid rights, contravened § 19.345(b) and was thus invalid as applied to Mr. Murphy. Accordingly, Oak Crest could not discharge Mr. Murphy, because he did not violate Section 8.11 of his Residence Agreement.

It is important to remember that this holding is limited to an application of Maryland law to nursing home facilities and continuing care retirement communities' nursing home care wings. The court noted in its discussion that, "as the Circuit Court restricted itself to the State law issue in entering the summary judgment, we shall do likewise." Oak Crest's Agreement provisions were only held invalid under Maryland Code HG § 19.345(b). Accordingly, elder law attorneys should be familiar with their own state's statutes that protect the rights of nursing home applicants to seek Medicaid assistance.

The Oak Crest decision will not apply to residents of Maryland CCRCs who initially enter the assisted living or independent living wings. The court stated, "If a person such as Ruth moved into an independent or assisted living unit pursuant to a CCRC Residence and Care Agreement containing such a provision, [as Section 8.11] there would be no conflict with § 19.345(b) and she would, indeed, be precluded from unilaterally transferring assets so as to deplete her net worth."

Recent developments in Congress, however, will have a major impact on this issue. Effective February 8, 2006, section 6015 of the Deficit Reduction Act of 2005⁴ amends 42 U.S.C. § 1396r(c)(5) as follows:

(v) TREATMENT OF CONTINUING CARE RETIREMENT COMMUNITIES ADMISSION CONTRACTS. - Notwithstanding subclause (II) of subparagraph (A)(I), subject to subsections (c) and (d) of section 1924, contracts for admission to a State licensed, registered, certified, or equivalent continuing care retirement community or life care community, including services in a nursing facility that is part of such community, may require residents to spend on their care resources declared for the purposes of admission before applying for medical assistance.⁵

As a result of the Deficit Reduction Act of 2005, the states must review and modify their laws and

⁴Opponents of the Deficit Reduction Act of 2005 are weighing a court challenge on the grounds that the act is unconstitutional. At issue is a provision involving the period of time the government pays to rent some types of durable medical equipment. The Senate voted for 13 months, as intended by Conference Committee, but a Senate clerk erroneously put down 36 months in sending the bill back to the House for a final vote, and that's what the House approved. By the time the bill was sent to President Bush, the number had been changed back to 13 months as passed by the Senate but not the House. The constitutional question is based on the fact that a bill can only become a law if the House and Senate pass it in identical form.

⁵Deficit Reduction Act of 2005, Conference Report to Accompany S. 1932, § 6015 (a).

regulations as necessary so as not to conflict with this change in federal law.

Elder law attorneys can learn several lessons from this case. First, attorneys must be cognizant of the current federal and state statutes concerning nursing home and CCRC residence and care agreements. Second, attorneys must be familiar with the residence contracts used by nursing home facilities and CCRC's in their geographic area of practice. Ideally, attorneys should review such contracts before the clients or their agents sign them. Finally, attorneys must appropriately advise clients who apply to nursing homes and CCRCs.

Beverly Healthcare Brandywood v. Betty L. Gammon, et al. (2005)⁶

The Court of Appeals of Tennessee, that state's intermediate appellate court, affirmed a trial court's ruling that a nursing home resident's cash gifts to his children, made pursuant to an Elder Law attorney's plan, were considered fraudulent transfers under the relevant state statutes, and that the resident's children were required to reimburse the nursing home for their deceased father's unpaid nursing home bills. The children were also required by the terms of their father's nursing home contract to reimburse the nursing home for its attorney's fees incurred in the suit against them.

This case arose when Beverly Healthcare Brandywood ("Brandywood") filed suit against the three daughters of Charles Leath to collect on a judgment arising from Mr. Leath's nursing home debts. Brandywood had not been able to collect the funds from Mr. Leath or his estate, and thus instituted proceedings against his three daughters, under the theory that the gifts made by Mr. Leath to his daughters were fraudulent transfers.

Mr. Leath had lived in Brandywood and received Medicaid assistance. He had three daughters, owned his home, and planned to return to it. Under Tennessee law, the home was an exempt asset. Nevertheless, following the advice of an Elder Law Attorney, Mr. Leath sold his home to one of his daughters for \$69,000 (fair market value), and he gifted \$27,500 of the resulting cash proceeds to his daughters. He also gave an additional \$5,000 to each daughter under a "Service and Life Care Agreement." These gifts and transfers totaled approximately \$42,500, leaving Mr. Leath with countable resources well in excess of the \$2,000 Medicaid limit.

Mr. Leath was subsequently found ineligible for Medicaid because of his excess resources and the gifts. His daughters used most of the available gifted funds to privately pay for their father's care until his death. At Mr. Leath's death, however, Mr. Leath still owed approximately \$10,000 for unpaid nursing home expenses. Brandywood was unsuccessful in collecting this sum from Mr. Leath's estate, and so the facility filed suit against Mr. Leath's daughters under a fraudulent transfer theory.

⁶Beverly Healthcare Brandywood v. Betty L. Gammon, et al., No. M2003-03117-COA-R3-CV

The Tennessee Court of Appeals discussed the relevance of three Tennessee code sections⁷:

Every conveyance made and every obligation incurred by a person who is or will be thereby rendered insolvent is fraudulent as to creditors without regard to such person's actual intent, if the conveyance is made or the obligation is incurred without a fair consideration.⁸

Every conveyance made and every obligation incurred without fair consideration, when the person making the conveyance or entering into the obligation intends or believes the debts will accrue beyond the party's ability to pay as they mature, is fraudulent as to present and future creditors.⁹

Every conveyance made and every obligation incurred with actual intent, as distinguished from intent presumed in law, to hinder, delay, or defraud, either present or future creditors, is fraudulent as to both present and future creditors.¹⁰

The Court of Appeals held that Mr. Leath's transfers to his daughters were not fraudulent under Tenn. Code Ann. § 66-3-305, because Mr. Leath was not rendered insolvent at the time of the transfers. He had retained over \$14,000 in his account; this was sufficient to fulfill his debts at that time.

The Court, however, held that Mr. Leath's transfers of \$27,500 in gifts to his daughters were fraudulent under Tenn. Code Ann. § 66-3-307, because first, the transfers were not supported by consideration, and second, Mr. Leath had reason to believe his future debts would exceed his ability to pay them, because he was rendered ineligible for Medicaid by the sale of his home, and as a result was privately paying for his care with limited funds.

The Court also held that Mr. Leath's transfers of \$27,500 in gifts to his daughters were fraudulent under Tenn. Code Ann. § 66-3-308 because, first, the transfers were not supported by consideration, and second, Mr. Leath made the transfers with the intent of having Medicaid be responsible for his debts.

The Court upheld the trial court's award of attorney's fees to Brandywood, noting the parties' contract awarded attorney fees. The contract, in part, provided:

⁷ The Tennessee legislature repealed these statutes in 2003 and adopted the Uniform Fraudulent Transfer Act. ("UFTA") The UFTA is similar to the repealed statutes; hence the Court would have likely reached the same holding under the UFTA.

⁸ Tenn. Code Ann. 66-3-305 (Supp. 199)(repealed 2003).

⁹ Tenn. Code Ann. 66-3-307 (Supp. 199)(repealed 2003).

¹⁰ Tenn. Code Ann. 66-3-308 (Supp. 199)(repealed 2003).

In the event the Facility institutes and is a prevailing party in litigation against any party to this Agreement, arising from that party's failure to comply with the terms of this Agreement, the Facility shall be entitled to receive from the losing party reasonable attorney's/collection agency fees.

The court indirectly addressed the argument that this contract provision should not apply to Mr. Leath's daughters because they were not a "party to [the] Agreement." The court noted that Brandywood's legal expenses were incurred in collecting on its judgment against Mr. Leath's estate. Mr. Leath caused Brandywood to pursue his daughters when he transferred funds to them. Hence, the court found the parties' contract entitled Brandywood to be reimbursed for its attorney's fees spent in pursuing Mr. Leath's daughters to satisfy its judgment against their father's estate.

This case arose because a nursing home's bills remained unpaid. The resident gifted resources that rendered him ineligible for Medicaid assistance, and he was unable to pay all of his subsequent nursing home bills. His estate was also unable to satisfy his debts. The nursing home pursued the resident's daughters under a fraudulent transfer theory.

It is critical that elder law attorneys ensure their clients leave no unpaid debts and nursing home bills, because this Court made it very clear that it considered the use of an elder law attorney evidence of a fraudulent intent to avoid creditors:

The Court specifically finds that the defendants embarked upon a design, not of their own making, but a design developed by a professional that they relied upon, in order to protect their father's assets. The defendants were reluctant to lose all of their father's assets to legitimate creditors such as a nursing home or Medicare and not have anything left over to take care of the final needs of their father and perhaps nothing to be disbursed among themselves.

The Court also finds evidence of several badges of fraud connected to the transfers: (i) the relationship of the parties; (ii) the fact that virtually all of Mr. Leath's property was given away in a span of some forty days; (iii) the precarious financial position of Mr. Leath; and (iv) the denial of Medicaid benefits. These badges of fraud create a conclusive presumption of fraud and shift the burden going forward on the defendants. The defendants failed to offer any innocent purpose for the transfers. The only apparent purpose for the transfers was to somehow have Medica[id] pay for all of their father's care without having to consume any of their father's assets.¹¹

Elder law attorneys can best protect their clients from such claims by ensuring that their client's debts, including nursing home bills, are fully paid, particularly if a gifting strategy is used. While no attorney intentionally plans to leave unpaid nursing debts, this Court, as shown above, makes

¹¹ See Fn. 5.

clear the existence of such debts can incur recovery under a fraudulent transfer theory. Therefore, an attorney's Medicaid plan, made in good faith, and which accounts for all of a client's debts, could yet be fraudulent if it results in unpaid bills. Consequently, attorneys must carefully plan their client's Medicaid strategies.

The Supreme Court of North Dakota has also applied fraudulent transfer rules to certain transfers of assets in a Medicaid estate recovery context.¹² In Estate of Bergman, the North Dakota Supreme Court held that the State's Department of Human Services ("DHS") was entitled to recover from the estate of Mrs. Bergman. During his life, Mr. Bergman had gifted funds to his wife and subsequently became eligible for Medicaid. After her husband's death, Mrs. Bergman became terminally ill and made gifts to her children after being advised that the DHS could recover from her estate for Medicaid benefits paid to her deceased husband. After Mrs. Bergman's death, the DHS filed a claim against her estate for Medicaid benefits paid to her husband. The Court first discussed prior North Dakota cases that permit DHS to trace assets from an institutionalized spouse to a community spouse, in order to recover against the community spouse's estate. The Court concluded that DHS was authorized to trace the assets formerly held by Mr. Bergman, and recover from Mrs. Bergman's estate. Because Mrs. Bergman's estate was insolvent because of the transfers, the Court further held Mrs. Bergman's transfers to her children were a fraudulent attempt to avoid Medicaid recovery. The Court voided the transfers and held the DHS was entitled to recover from the transferred assets:

Although those assets may not have been in Lucille Bergman's estate when she died, she purported to gift those assets to her children in contemplation of death and after being informed of a possible claim by the Department. Under N.D.C.C. § 30.1-18-10, a personal representative may recover property transferred by the decedent to avoid the decedent's creditors...Under N.D.C.C. § 13-02.1-05(1) of the Uniform Fraudulent Conveyance Act, a debtor's transfer of property is constructive fraud as to a creditor if the debtor made the transfer without receiving reasonably equivalent value...and the debtor was insolvent at the time of, or became insolvent as a result of, the transfer.¹³

More jurisdictions may follow the Brandywood and Bergman decisions and apply fraudulent transfer rules to similar transfers of assets. Elder law attorneys¹⁴ should be mindful of this precedent and advise their clients to retain sufficient funds to pay all nursing home charges incurred

¹² Estate of Bergman, 2004 ND 196, 688 N.W.2d 187 (2004)

¹³ Id.

¹⁴ Additionally, when assisting clients with Medicaid planning, Elder Law attorneys should consider their potential exposure to liability. Little precedent exists regarding liability of an attorney for assisting a client in a transfer that is held to be in defraud of creditors. A few courts have found attorneys liable for certain fraudulent transfers. See McElhaonon v. King, 728 2d 273 (Arizona, 1986); Durant Software v. Herman, 220 CA3d 460 (1989). The attorneys in these cases were held liable for deliberately assisting their clients in avoiding judgment creditors.

during periods of Medicaid ineligibility. Elder law attorneys should additionally advise their clients and their families of the risk that the state may use this precedent in a Medicaid estate recovery action. In some states, if the state Medicaid agency is permitted to trace assets transferred from an institutionalized spouse to a community spouse for purposes of estate recovery, the transferred assets are not necessarily the community spouse's assets to dispose of as he or she pleases. Whether or not asset transfer laws are changed, we should not be surprised to see further challenges to Medicaid asset transfers by states and nursing homes.