Congressional Research Service

Medicaid Estate Planning and Legislative Options Testimony Before the Senate Special Committee on Aging

July 20, 2005

Julie Stone-Axelrad
Analyst in Social Legislation
Domestic Social Policy Division

Good afternoon Senator Smith, Senator Kohl and Members of the Committee. My name is Julie Stone-Axelrad and I am a health policy analyst at the Congressional Research Service. My testimony today deals with the issue of Medicaid estate planning, a means by which some elderly people divest their income and assets both to qualify for Medicaid sooner than they otherwise would and to protect their assets from estate recovery.

As you know, the Medicaid program is means tested. It covers about 54 million people across the nation. Although the program is targeted toward low-income individuals, not all of the poor are eligible, and not all of those covered are poor. Medicaid beneficiaries include children and families, people with disabilities, pregnant women, and the elderly.

Today's discussion about Medicaid estate planning focuses on a subset of Medicaid beneficiaries age 65 and over who need long-term care and have income greater than the Supplemental Security Income program's cash benefit of $579 a month. Medicaid law allows states to cover people whose income reaches, or is sometimes greater than, about 218% of the federal poverty level, but only if they require the level of care that is offered in a nursing home. States may also extend coverage to people who have medical expenses that deplete their income to specified levels. Once eligible for Medicaid, beneficiaries are required to apply their income above certain amounts toward the cost of their care.

In addition to income, individuals must also meet states' asset standards to qualify for Medicaid. These standards usually follow SSI program rules and generally allow individuals to retain $2,000 in countable assets as well as certain types of noncountable or exempt assets, such as a home or car of unlimited value, and certain types of trusts.

Other rules apply to married couples in which one person seeks Medicaid long-term care and the other does not. These rules are intended to prevent impoverishment of the spouse not seeking Medicaid by allowing him or her to retain higher amounts of income and assets than the allowed for Medicaid beneficiaries.

Not all Medicaid beneficiaries have engaged in estate planning. Some people meet Medicaid's eligibility requirements because their initial income and assets are equal to or below a state's specified thresholds. Some reach the thresholds after depleting their income and assets on the cost of their care, thus "spending down." My testimony today is about a third category of people who divest their assets to qualify for Medicaid. We do not have sufficient data to assess the number of people in each of these groups.

To ensure that Medicaid applicants do not give away assets to gain eligibility sooner that they otherwise would, Congress established asset transfer rules that impose penalties on applicants who either give away or transfer their assets for less than the market price. Specifically, the rules require states to delay coverage of nursing home care and other long-term care services for certain individuals who apply for Medicaid after improperly disposing of assets on or after a look-back date.

I mentioned earlier that beneficiaries are allowed to retain certain assets and still qualify for Medicaid. Medicaid's estate recovery program is intended to enable states to recoup these private assets from the estate of a beneficiary upon the person's death. Under federal law states are required to recover the amounts they spend on long-term care services from the beneficiary's probate estate, which often includes the home, if there is one. If states choose, they may go beyond the probate estate to collect other assets as well, such as those that may have a designated beneficiary, like an annuity or trust. But not all states do this.

Despite Congress' efforts to discourage Medicaid estate planning through the design of eligibility, asset transfer, and estate recovery provisions, current law does not preclude all available means people may use to protect assets. A variety of methods may still be used to avoid estate recovery or to obtain Medicaid coverage while using personal resources for other purposes, such as giving gifts to children or protecting assets for an inheritance. The following are some examples of techniques that people may use to divest assets.

Minimize the Impact of the Penalty Period

First, people may transfer assets to minimize the impact of the penalty period. Medicaid law specifies that penalties for improper transfers begin on the first day of the month in which assets are transferred. These penalties are periods of ineligibility, in months, for certain long-term care services. People could transfer a part of their assets while keeping enough to pay for their care during the ineligibility period.

Avoid Penalties by Transferring Assets Outside the Look-Back Period

Second, people may transfer funds sufficiently in advance of the look-back period to avoid penalties. Any transfers made within 36 months of application to Medicaid, and 60 months for certain trusts, are subject to penalties. Any transfers made prior to these look-back periods are not subject to penalties.

Convert Countable Assets into Non-Countable Assets and Income

Third, people may convert countable assets into noncountable assets or income, such as using money in a savings account to purchase an annuity for fair market value.

Use Funds Above Medicaid Thresholds for Any Purpose

Fourth, people may use assets above Medicaid thresholds for any purpose. For example, if individuals have $10,000 and the state's asset threshold is $2,000, then to become eligible individuals must deplete the excess $8,000. They can either spend the $8,000 on the cost of their care or on anything else they choose, such as home improvements or personal items to maintain a certain living standard.

In addition to these techniques, a married couple could divorce and give all of their assets and income to the spouse not seeking Medicaid. An other option would be for a spouse to refuse to provide financial support for the spouse seeking Medicaid.

A number of these methods are probably unintended consequences of provisions in Medicaid law, designed to assist certain people who have low-income, or who have high medical or long-term care expenses. The availability of these methods under current law also reflects a lack of consensus about the amount of assets that should be held by people who face high long-term care costs before qualifying for Medicaid. In addition, the law likely reflects the difficulty in writing legislative language to discourage all methods for transferring assets without inadvertently restricting access to Medicaid's safety net.

Considerations for Legislation

A variety of policy options have been proposed to discourage Medicaid estate planning and the improper transfer of assets. When evaluating which legislative options, if any, to adopt, there are some policy questions you may want to consider.

First, tightening Medicaid laws regarding eligibility and asset transfers will likely deter people from deliberately manipulating the rules to qualify for Medicaid. Such changes, however, are likely to impose stricter penalties on people who made transfers without any intention of ever needing Medicaid's assistance. You may want to consider how you want the law to treat people in this latter group.

Second, who will actually pay for the care of elders when Medicaid won't? One possibility is that beneficiaries would pay for their own care during the penalty period by either recovering their transferred funds or liquidating any exempt assets they may have to pay for care. Another possibility is that providers, such as nursing homes, will assume more cases of uncompensated care, either reducing the profits of proprietary homes, or relying more heavily on the charitable donations of not-for-profit homes. Others may rely on informal caregivers to provide the care they need, and still others may forgo care altogether.

Third, you may want to consider the high costs of long-term care services, often reaching over $60,000 a year for a private stay in a nursing home. If changes to current law result in further restricting access to Medicaid's long-term care coverage, what, if anything, should be done to assist older persons with these costs?

Finally, it is unlikely that the adoption of just one or two of the policy options currently being discussed will lead to significant reductions in Medicaid estate planning. It is likely that narrow changes to current law will still allow people to find ways to divest assets. To achieve significant reductions in Medicaid estate planning, a package of changes is more likely needed. In designing such a package, you may consider measures to make transferring assets more difficult, measures to strengthen penalties for people who make inappropriate transfers, as well as measures that provide a safety net for applicants for whom the state determines that significant hardship could result without Medicaid's assistance.

At the request of the Committee, I have prepared some comments on some of the legislative options that have been proposed.

Changing the Penalty Period

One option is changing the beginning of the penalty period from the time the Medicaid applicant made the asset transfer to the time the applicant is determined eligible for Medicaid.

The proposal could increase the likelihood that people who improperly transfer assets will be penalized, possibly serving as a stronger deterrent to such transfers. Strengthening the penalty period could either delay or even prevent Medicaid from paying for care of certain individuals, thus potentially incurring savings to the Medicaid program. On the other hand, providers may end up paying for care not paid for by Medicaid and some people might not be able to obtain the care they need. These implications may have unintended consequences on provider budgets and access to care.

Extending the Look-Back Period

Another option would be to extend the look-back period for transferred assets beyond the three to five-year period in current law. This would require people who want to divest assets and avoid the penalty period to plan even earlier than they must under current law, making it more difficult. A longer look-back period could lead states to identify more transfers, and thus impose more penalties. Savings to Medicaid might be found.

However, the farther into the past the transfer was made, the less likely the applicant may be to recover the transferred funds to pay for care during the penalty period. Extending the look-back period could also place an additional administrative burden on eligibility workers, slowing down the process as workers review and try to obtain past financial documents from applicants.

Other legislative options include:

- Placing a universal cap on the value of all exempt assets;
- Counting assets not currently counted;
- Requiring applicants to apply a portion of their home equity to the cost of their care before Medicaid will pay for care; and
- Requiring an applicant to make the state the beneficiary of any remaining funds of an exempt asset after the beneficiary's death.

Each of these proposals could reduce the total amount of assets that could be protected either at the point of application to the Medicaid program or at the point of estate recovery upon a beneficiary's death. However, there would still be no guarantee that funds above the protected amounts would be used to pay for the cost of care.

Since each of these options would target a different method people might use to protect assets, together they represent a more comprehensive approach to addressing Medicaid estate recovery. On the other hand, without more information about which methods are most commonly used, we do not know which options would be most effective and which, if any, might have unintended implications on access to care.

Finally, there are insufficient data available to accurately estimate the prevalence of asset transfers today and none that can reasonably predict whether or how much this incidence might grow in the future. We do know that a significant amount of anecdotal evidence exists about persons engaging in Medicaid estate planning. We also know that an industry of elder lawyers specializing in Medicaid has developed across the nation. Court cases at federal and state levels also point toward the prevalence of transfers. In addition, we know that states have expressed a strong interest in curbing Medicaid estate planning and have taken a number of measures to try to do so.

Any protection of assets that results in Medicaid paying for care that would otherwise have been paid with private funds increases Medicaid's program costs. Unfortunately, without better data we cannot accurately estimate how much Medicaid estate planning costs the program now and how much savings could be generated from further restricting transfers in the future. Although changes to current law could deter people from transferring assets, strengthen penalties for doing so, and possibly increase the likelihood that private funds would be used to pay for care, it is still unclear how such changes might impact access to care for older persons with long-term care needs.