

# ELDERLAW

## NEWS

New Jersey

Legal News for the Aging and Disabled

September 2005

### **RECENT CASE LAW DEVELOPMENTS: NEW JERSEY COURTS PUT AN END TO MEDICAID'S RESTRICTIVE TREATMENT OF CERTAIN ANNUITIES**

As discussed in the previous issue of the Elderlaw News, any valid estate or asset protection plan must be based on current federal and state law. However, public benefits laws, particularly Medicaid, are in a constant state of flux, which in turn may affect your estate or asset protection plan.

An article in the March 2005 edition of the Elderlaw News discussed the New Jersey Appellate Division case of *Estate of DeMartino v. Division of Medical Assistance and Health Services*, 373 N.J. Super. 210 (App. Div. 2004), cert. den., 182 N.J. 425 (2005), which for the first time permitted the Division of Medical Assistance and Health Services ("DMAHS") to assert a lien for the recovery of Medicaid benefits against the assets of a testamentary trust established for the benefit of a Medicaid recipient by his late wife.

Following the issuance of that opinion, the New Jersey Appellate Division issued two decisions that impact on Medicaid's treatment of certain annuities. These two cases, *Estate of F.K. v. DMAHS*, 374 N.J. Super 126 (App. Div.), cert.

den., 184 N.J. 209 (2005) and *A.B. v. DMAHS*, 374 N.J. Super 460 (App. Div., Jan. 21, 2005), cert. den., 185 N.J. 38 (2005) both concern Medicaid's treatment of commercial annuities purchased for the benefit of a "community spouse" (the spouse of the Medicaid recipient/applicant). You should discuss these important decisions with your el-

**MANY OF THE FORMER ROADBLOCKS PREVENTING THE USE OF COMMERCIAL ANNUITIES AS PART OF AN ESTATE/ASSET PROTECTION PLAN HAVE NOW BEEN ELIMINATED BY RECENT CASE LAW.**

der law attorney when formulating your estate/asset protection plan; if you already have an estate/asset protection plan in place, you should be aware that the cases discussed below might affect your plan.

As discussed in detail below, the annuities in question in the recent cases of *F.K.* and *A.B.* were "actuarially

sound" commercial annuities. Medicaid's treatment of these annuities was challenged on three fronts. The first is Medicaid regulation N.J.A.C. 10:71-4.10(p)2i, which defines a commercial annuity purchased for the benefit of a community spouse as a countable "resource" to the extent that its purchase price exceeds the community spouse resource allowance ("CSRA"). The second is Medicaid's position that such an annuity is an "available asset" because it is readily marketable on the secondary market. The third is the requirement set forth in Medicaid regulations N.J.A.C. 10:71-4.10(b)(8) and -4.10(f), which mandate that the State of New Jersey be named as the first remainder beneficiary on such annuities. Each of these three challenges was successful, and our appellate court concluded that New Jersey Medicaid's current restrictive treatment of these annuities is impermissible.

#### **"Actuarially Sound" Annuities and the Community Spouse Resource Allowance**

According to Medicaid's

(Continued on Page 2)

(Continued from page 1)

federal Health Care Financing Administration Transmittal No. 64, whether the purchase of an annuity is penalized by Medicaid (as a transfer of assets for less than fair market value) is based upon whether the annuity is “actuarially sound”:

Annuities, although usually purchased to provide a source of income for retirement, are occasionally used to shelter assets so that individuals purchasing them can become eligible for Medicaid. In order to avoid penalizing annuities validly purchased as part of a retirement plan but to capture those annuities which abusively shelter assets, a determination must be made with regard to the ultimate purpose of the annuity (i.e., whether the purchase of the annuity constitutes a transfer of assets for less than fair market value). **If the expected return on the annuity is commensurate with a reasonable estimate of the life expectancy of the beneficiary, the annuity can be deemed actuari-**

**ally sound....** If the individual is not reasonably expected to live longer than the guarantee period of the annuity, the individual will not receive fair value for the annuity based on the projected return. In this case, the annuity is not actuarially sound and a transfer of assets has taken place, subjecting the individual to a penalty.

But despite the fact that federal Transmittal No. 64 directs that Medicaid’s treatment of annuities be based upon whether the annuity is actuarially sound, New Jersey regulation N.J.A.C. 10:71-4.10(p)2i attempted to place a further limitation on the purchase of such annuities for the benefit of the community spouse. That additional limitation was based upon the CSRA limit.

When one spouse applies for Medicaid benefits, the CSRA is that portion of a couple’s assets that is reserved for the benefit of the community spouse, calculated as one-half of the couple’s total joint and separate resources (subject to a ceiling of \$95,100 in 2005). The CSRA is considered unavailable to the Medicaid applicant spouse when determining Medicaid eligibility, but any amount above the CSRA must be spent before the Medicaid applicant will become eligible

for Medicaid.

Pursuant to N.J.A.C. 10:71-4.10(p)2i, in addition to requiring that an annuity be actuarially sound to escape a Medicaid penalty, New Jersey attempted to cap the amount that could be used to acquire an actuarially sound annuity at the CSRA limit.

In *F.K.*, an institutionalized husband and his wife had purchased an actuarially sound annuity in which his wife was the sole beneficiary of the income. Because the purchase price of the annuity was in excess of the CSRA, the annuity was deemed a countable asset and the husband was denied Medicaid eligibility based upon N.J.A.C. 10:71-4.10(p)2i. On appeal, the *F.K.* court accepted Transmittal No. 64 as “warranting deference.” According to Transmittal No. 64, if an annuity can be deemed actuarially sound, then it is a purchase for fair market value and cannot be subject to a Medicaid penalty period. Therefore, the court concluded that N.J.A.C. 10:71-4.10(p)2i’s CSRA cap is inconsistent with federal law and is invalid.

In *F.K.*, the DMAHS next argued that such an annuity is a “countable resource” because it has a market value in the secondary market. However, the *F.K.* court found that

(Continued from page 1)

“the marketability and value of

(Continued on page 3)

the income stream to [the wife] blurs the distinction between resource allocation and income allocation under the federal Medicaid law.” It also concluded that “there is no evidence in the record supporting the ... existence of a viable secondary annuities market or whether F.K. [and his wife] could sell the annuity or the income stream on such a market.”

In the *A.B.* case, after noting its “complete[] agree[ment]” with the *F.B.* decision, the Appellate Division went a step further by invalidating another New Jersey regulation regarding the treatment of annuities. Pursuant to N.J.A.C. 10:71-4.10(b)(8) and -4.10(f), New Jersey had placed an additional requirement for the acceptance of an annuity as a non-countable asset: the State of New Jersey was required to be named as the first remainder beneficiary on commercial annuities purchased for the benefit of the community spouse.

In *A.B.*, the husband of the institutionalized spouse had purchased a commercial, actuarially sound annuity in which he was the income beneficiary. However, the annuity named his daughter as the beneficiary upon his death. When the husband refused to name the State of New Jersey as first remainder beneficiary, the wife was denied Medicaid benefits.

The State defended its position requiring the naming

of the State as first remainder beneficiary as “essentially a form of leniency” which permits a Medicaid applicant the benefit of an annuity for the community spouse when it would have otherwise been considered a community resource. However, after accepting the reasoning of *F.K.* and finding that the State cannot consider as an available resource an actuarially sound commercial annuity purchased for the benefit of the community spouse (even if purchased with an amount in excess of the CSRA), the *A.B.* court concluded that the State’s justification for the beneficiary designation was unjustified.

Again, as in *F.K.*, the *A.B.* court rejected the state’s claim that the income stream for a commercial annuity has a resale value in the secondary market, finding that “there is no legally competent evidence in the record that there is a resale market for the income stream from these annuities. It went on to reason that,

even if there were legally competent evidence of a secondary market, the agency produced no proof of the resale value of [the] annuity. That annuity was purchased for approximately \$77,000. However, the resale value of an income stream

payable to an elderly annuitant during his anticipated remaining lifetime would certainly not be \$77,000. It might be a few cents on the dollar. Absent proof of the resale value, if any, of the income stream from the annuity, the agency could not conclude that *A.B.*’s spouse had assets beyond those allowed to the community spouse.

### Conclusion

The State of New Jersey filed appeals of both the *F.K.* and *A.B.* cases in the New Jersey Supreme Court. However, the Supreme Court denied both appeals. Thus, the issue of the viability of an actuarially sound annuity as an estate/asset protection plan option is resolved.

The *F.K.* and *A.B.* cases greatly expand the permissible use of commercial annuities as part of a Medicaid plan. Thanks to these new cases, a commercial, actuarially sound annuity is now a viable option among estate/asset protection plans that should be discussed with your attorney. ☒

## *Law Offices of Donald D. Vanarelli*

The Law Firm of Donald D. Vanarelli, with offices in Westfield, NJ and other conference locations convenient for our clients, is a unique law firm providing a broad range of legal services for the elderly, the disabled and their families. Because we concentrate on law for the elderly and disabled, we are especially sensitive to the stresses that America's confusing estate tax laws, public benefits laws and health care system can place on our clients and their families. To help ease this process, we offer these services:

Comprehensive Life Care Planning  
Estate Planning and Administration  
Mediation Services  
Social Security Disability Appeals  
Nursing Home Law and Litigation

Medicaid and Public Benefits Planning  
Guardianship and Fiduciary Services  
Medicare and Medicaid Appeals  
Medicaid Applications  
Special Needs Planning

### ★ **ANNOUNCEMENT OF ADDITION TO PROFESSIONAL STAFF** ★

The Law Office of Donald D. Vanarelli is pleased to announce the addition of a new professional staff member to the firm. **Margaret M. Corcoran, Esq.** obtained her law degree from Seton Hall University in 1998 after having earned masters degrees in education and the arts from Columbia University (1987) and a Master of Science degree from St. John's University (1977). Margaret worked for Morgan Stanley as a legal analysts. She also worked as an attorney in a law firm concentrating on elder law, estate planning and administration. Margaret joins Attorneys Donald D. Vanarelli and Whitney W. Bremer and an excellent support staff in the effort to provide elder law and estate planning services with excellence in legal expertise, compassion and sensitivity.

### ★ **Fall 2005 Elder Law Seminar Dates and Locations** ★

**Topic: Asset Protection Planning. In these seminars, you will learn how to protect your life savings from the catastrophic costs of care in an assisted living facility or a nursing home.**

<u>DATE</u>	<u>TIME</u>	<u>LOCATION</u>
October 12	7 p.m.	Law Firm, Westfield, NJ
October 25	1 p.m.; 7 p.m.	Henry Inman Library, Colonia, NJ
November 2	1 p.m.	Westfield Municipal Bldg.
November 3	7 p.m.	Westfield Municipal Bldg.
November 16	1 p.m.; 7 p.m.	Law Firm, Westfield, NJ

*Advance Registration Required, by calling: 908-232-7400, or by email: [dvanarelli@dvanarelli.com](mailto:dvanarelli@dvanarelli.com)*

## **ELDERLAW** **NEWS**

**LAW OFFICES OF  
DONALD D. VANARELLI**  
242 St. Paul Street  
Westfield, NJ 07090  
Tel: (908) 232-7400  
Fax: (908) 232-7214  
Email: [dvanarelli@dvanarelli.com](mailto:dvanarelli@dvanarelli.com)  
Websites: [dvanarelli.lawoffice.com](http://dvanarelli.lawoffice.com)  
-and- [elderlawanswers.com/attorney/vanarelli.html](http://elderlawanswers.com/attorney/vanarelli.html)

### **Recent Case Law Developments: New Jersey Courts Put An End To Medicaid's Restrictive Treatment of Certain Annuities**