State of New Jersey

OFFICE OF ADMINISTRATIVE LAW

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A copy of the administrative law judge's decision is enclosed.

This decision was mailed to the parties on FEB 27 2009

State of New Jersey
OFFICE OF ADMINISTRATIVE LAW

INITIAL DECISION
OAL DKT. NO. HMA 7536-08

E.F.,

Petitioner,

v.

DIVISION OF MEDICAL ASSISTANCE AND HEALTH SERVICES AND UNION COUNTY BOARD OF SOCIAL SERVICES,

Respondents.

Donald D. Vanarelli, Esq., on behalf of petitioner

Dianna Rosenheim, Deputy Attorney General, on behalf of respondents (Anne Milgram, Attorney General of New Jersey)

Record Closed: February 6, 2009 Decided: February 26, 2009

BEFORE **WALTER M. BRASWELL**, ALJ:

STATEMENT OF THE CASE AND PROCEDURAL HISTORY

Petitioner E.F. appeals the denial by respondents Division of Medical Assistance and Health Services and Union County Board of Social Services (UCBSS or County) of her request for Medicaid nursing home benefits. The denial dated May 29, 2008, was based on the County's determination that the petitioner's resources exceeded the

community spouse's protected resource share of $106,400. On June 10, 2008, the petitioner requested a fair hearing, and the case was transmitted to the Office of Administrative Law, where it was filed on June 30, 2008. N.J.S.A. 52:14B-1 to -15; N.J.S.A. 52:14F-1 to -13. A hearing was scheduled for August 4 and November 19, 2008, before Walter M. Braswell, ALJ, but was adjourned with the consent of both parties. The parties agreed to have the case decided on a summary basis and submitted briefs and uncontested statements of fact in lieu of a hearing. I concurred with counsel and on February 6, 2009, upon receipt of the Stipulation of Uncontested Facts, the record closed.

FACTUAL DISCUSSION

The parties stipulated to the following, which is **FOUND as FACT**:

1. E.F. was born on June 1, 1929, and was seventy-nine (79) years of age at the time of her death in 2008. E.F. and D.F. were married on October 27, 1951. At the time of her Medicaid application, E.F. was suffering from Parkinson's disease, depression, COPD and had suffered congestive heart failure.

2. D.F. was appointed as guardian of E.F. on June 8, 2006.

3. On June 29, 2006, as guardian of E.F. and on his own behalf, D.F. transferred their marital home located at 747 Beverly Road, Rahway, New Jersey from D.F. and E.F., husband and wife, to D.F., married. The deed was recorded on July 10, 2006.

4. E.F. became a resident of Genesis Eldercare, Westfield Center located at 1515 Lamberts Mill Road, Westfield, NJ 07090-4763 on January 19, 2007, where she remained until her death.

5. On April 30, 2007, D.F. used money from his Ameritrade IRA, account number 419-99063-1-6, to purchase an annuity from Jefferson-Pilot Life

Insurance Company (the annuity or the Freeland annuity). In or about April 21, 2007, D.F. signed an "Amendatory Endorsement" stating that the [D.]F. annuity policy is "irrevocable and immediate," that the policy "cannot be transferred, surrendered or assigned," and that the policy "has no cash value." Further, on or about May 14, 2007, D.F. also signed a Policy Disclosure form wherein he agreed that the payments from the annuity could not be commuted, advanced or accelerated.

6. Also on May 30, 2007, an application for nursing home Medicaid benefits was filed on behalf of E.F.

7. The Ameritrade IRA Account used to purchase the annuity was a qualified individual retirement account (IRA) as defined in 26 U.S.C. § 408(a).

8. Although funds from his IRA were used to purchase the annuity, D.F.'s annuity application incorrectly identified the source of the premium as non-qualified.

9. In April 2008, D.F. had the clerical error regarding the annuity corrected, changing it from being labeled as non-qualified to qualified. At that time the 2007 Form 1099R was corrected.

10. The annuity contract itself does not contain any language specifying whether it was funded with non-qualified or qualified funds. The only documentation of this error is contained in the Policy Disclosure, which specifically states, "This Illustration is Not a Contract."

11. Dale M. Krause, Esq., the chief executive officer and founder of Krause Financial Services, LLC assisted D.F. in purchasing the F. annuity. Mr. Krause submitted a certification confirming that Lincoln has been unable to produce a corrected copy of the Policy Disclosure, setting forth the corrected qualified status, because of the merger between Jefferson-Pilot and Lincoln.

12. After filing her application on May 30, 2007, the state Medicaid agency wrote to E.F. in September and October 2007 for more information, but E.F. received no decision regarding her eligibility for Medicaid benefits for one year from the date she filed for benefits.

13. One year later, in a letter dated May 30, 2008, Medicaid denied E.F.'s application for benefits. The denial concluded that E.F. was ineligible because the face value of D.F.'s annuity was considered a countable resource, and rendered E.F. ineligible due to excess resources.

14. Medicaid's denial letter indicated that, if the F.s submitted three (3) quotes documenting the annuity's fair market value, the fair market value of the annuity would be used to determine the applicant's resource eligibility.

15. D.F. was born on June 23, 1924. On April 30, 2007, the date he purchased the annuity, his life expectancy was 6.41 years, or 76.92 months. Therefore, the annuity is actuarially sound pursuant to the requirements of HCFA 64, because it provided for 76 total months payments.

16. D.F.'s disabled adult child, De.F., through a testamentary trust under the Last Will and Testament of D.F. entitled the "[De.F.] Supplemental Benefits Trust," was designed as the primary beneficiary of the retirement annuity at the time of purchase. As of January 13, 2009, New Jersey's Department of Human Services, the state Medicaid agency, was designated as the first contingent beneficiary, up to the extent of medical assistance provided to the institutionalized individual. D.F.'s other children, N.C. and H.F., were designated as the second contingent beneficiaries. These beneficiary designations satisfy the requirements of the Deficit Reduction Act of 2005, which states that an annuity naming a disabled child as primary beneficiary, and the State as a remainder

beneficiary, is not deemed to be a transfer for less than fair market value. 42 U.S.C. § 1396p(c)(1)(F).

17. DMAHS provided a letter from Peachtree in which that company stated that it might not be able to proceed with the purchase: "There is an endorsement to this policy that may not [en]able us to complete the transaction if Lincoln objects to the change of ownership due to this." As set forth in petitioner's moving brief, three other companies have advised that they would not purchase a qualified annuity. DMAHS acknowledges that any purchase of the annuity would not be a purchase of the annuity contract itself, but would, in fact, be a purchase of the payment stream.

LEGAL ANALYSIS

The Medicaid program is governed by a combination of State and Federal law. Mistrick v. Div. of Med. Assistance and Health Servs., 154 N.J. 158, 165 (1998). The purpose of the program is to provide medical assistance to persons "whose resources are determined to be inadequate to enable them to secure quality medical care at their own expense." N.J.S.A. 30:4D-2. Thus, Medicaid benefits are a source of last resort and are available only after the applicant's own resources are deemed insufficient. Ibid.

The financial eligibility determination is based upon the resources of the applicant. N.J.A.C. 10:71-4.1. In examining the resources of a married couple where one individual is receiving institutional care, the board of social services looks to the combined countable resources of the couple, which include all resources owned by either member of the couple individually or together. N.J.A.C. 10:71-4.8(a).

Addressing a nearly identical situation as that presented in this case, the Appellate Division has noted that considering the marketable value of an income stream from an annuity to be a resource "blurs the distinction between resource allocation and income allocation under the Federal Medicaid law." F.K. v. Div. of Med. Assistance and Health Servs., 374 N.J. Super. 126, 144 (App. Div. 2005). Conversely, to do otherwise, and allow an annuity, and its income stream, to be excluded from the Medicaid eligibility

determination, is contrary to the purpose of the Medicaid program. See Mertz v. Houstoun, 155 F. Supp. 2d 415, 427 (D. Pa. 2001) (noting that annuities are used as a loophole to shield assets from the Medicaid eligibility determination).

Despite the fact that it is contrary to the purpose of the Medicaid program, the Mertz court held that "a couple may effectively convert countable resources into income of the community spouse which is not countable in determining Medicaid eligibility for the institutionalized spouse by purchasing an irrevocable actuarially sound commercial annuity for the sole benefit of the community spouse." Ibid. Quoting favorably from this decision, the F.K. court held that a New Jersey regulation using the community spouse resource allowance as a cap for the amount of funds a Medicaid applicant can use to purchase an annuity was inconsistent with Federal law. F.K., supra, 374 N.J. Super. at 146. This, decision, like Mertz, is premised on the idea that after the annuity is purchased, the purchaser no longer has an ownership interest in the funds and, consequently, the funds are no longer an available resource. (In the present matter, however, the UCBSS is not looking to establish the annuity itself as an available resource, but, instead, is looking to establish the funds received from the annuity – the income stream – as an available resource.)

In 1988, responding to a growing awareness of the plight of elderly spouses who were impoverished when the spouse upon whose income he or she relied was institutionalized (e.g., Schachner v. Perales, 648 N.E.2d 1321, 1322 (N.Y. 1995)), Congress enacted the Medicare Catastrophic Coverage Act (MCCA), 42 U.S.C.A. § 1396r-5, as amended by P. L. 100-360, 102 Stat. 683 (1988). Before the MCCA nearly all of a couple's assets had to be depleted before either individual could be eligible for Medicaid, leaving the spouse to remain in the community essentially destitute. H.R. Rep. No. 105 (II), 100th Cong., 2d Sess. 65-68 (1988), reprinted in 1988 U.S.C.C.A.N. 803, 888-92. Moreover, all income, including Social Security or one's private pension, was diverted to pay for institutional costs.

The MCCA community spouse provisions were enacted to "end this pauperization by assuring that the community spouse has a sufficient – but not excessive – amount of income and resources available to them while their spouse is in

a nursing home at Medicaid expense." 1988 U.S.C.C.A.N. at 888; see also Whitehouse v. Ives, 736 F. Supp. 368, 371 (D. Me. 1990) (request for relief from Medicaid eligibility rules rendered moot by MCCA).

> The goal of the MCCA was to ensure sufficient income and resources for the community spouse, while committing a fair share of their resources to the institutionalized spouse's care. To that end, the MCCA established a level of income and resources for the community spouse that is protected from inclusion when determining the institutionalized spouse's eligibility for Medicaid and which need not be spent down for the spouse's care.
>
> [A.K. v. Div. of Med. Assistance and Health Servs., 350 N.J. Super. 175, 179 (App. Div. 2002) (citations omitted).]

An applicant for the Medicaid Only program must meet financial eligibility requirements. N.J.A.C. 10:71-1.2(a). If the resources of the applicant and their spouse exceed $106,400, the applicant is ineligible. N.J.A.C. 10:71-4.8(a). N.J.A.C. 10:71-4.1(b) defines a resource "as any real or personal property which is owned by the applicant [or his spouse] and which could be converted to cash to be used for [the applicant's] support and maintenance." Such a resource must be available to an individual. N.J.A.C. 10:71-4.1(c). A resource is available when "[t]he person has the right, authority, or power to liquidate real or personal property, or his or her share of it." N.J.A.C. 10:71-4.1(c)(1). The UCBSS denial in this case is based on the contention that the annuity purchased by E.F. and D.F. are an available resource that exceed the permitted threshold.

Petitioner contends that the annuity cannot be liquidated because it is unmarketable, in that neither the annuity contract nor the income stream it generates is assignable. Consequently, the annuity is not a countable resource, but rather income. Moreover, the definition of income includes "payments received as an annuity." 42 U.S.C.A. § 1382a(a)(2)(B); see also N.J.A.C. 10:71-5.4(a)(3). Petitioner, therefore, argues that the income provided by the annuity is protected by the MCCA, which provides that "no income of the community spouse shall be deemed available to the institutionalized spouse." 42 U.S.C.A. § 1396r-5(b)(1).

The UCBSS counters that the annuity is a resource because, arguably, it may be sold on the secondary market, and, thus, converted to cash. Further, it is not specifically excluded as a resource by the regulations. N.J.A.C. 10:71-4.4(b). The UCBSS explains that while the annuity may also provide income, it must be first considered a resource because the couple has the right, power and authority to liquidate it and use it for the Medicaid applicant's care, and this is the first inquiry in the eligibility determination. The UCBSS maintains that an annuity should be viewed no differently than an investment vehicle such as shares of stock, a mutual fund or rental property, which would demand liquidation in order to meet resource limitation requirements to gain Medicaid eligibility.

Petitioner also maintains that the Deficit Reduction Act of 2005 (DRA), which supplemented the Omnibus Budget Reconciliation Act of 1993, permits a community spouse to shield resources by converting assets to income through the purchase of an annuity contract, so long as (1) the State is named as the first remainder beneficiary to the extent that the institutionalized spouse received Medicaid benefits, (2) the annuity is irrevocable and non-assignable, and (3) the annuity is actuarially sound. 42 U.S.C.A. § 1396p(c)(1)(F) and (G). The UCBSS refutes petitioner's contention and points to the language in the DRA which amended 42 U.S.C.A. § 1396p in providing:

> Nothing in this subsection shall be construed as preventing a State from denying eligibility for medical assistance for an individual based on the income or resources derived from an annuity described in paragraph (1).
>
> [42 U.S.C.A. § 1396p(e)(4).]

And 42 U.S.C.A. § 1396p(e)(1) refers to "any interest the individual or community spouse has in an annuity . . . regardless of whether the annuity is irrevocable or is treated as an asset." The UCBSS argues that in enacting the DRA, Congress intended to halt people with resources from cheating the system to get free medical care from a taxpayer-funded program for the poor by attempting to hide their assets in an annuity which will return the assets to them over time.

CURRENT CONTROLLING LAW

The United States Court of Appeals for the Third Circuit recently decided James v. Richman, 547 F.3d 214 (3d Cir. 2008). In James the circuit court held that payments from an annuity owned by the community spouse are income of the community spouse under 42 U.S.C. § 1396r-5[1] and that the State could not compel the community spouse to attempt to sell the income stream. The James court stated:

> Alternatively, the Department argues that Josephine James could create a new annuity, selling the right to an income stream that is equal to the income to which she is entitled from the existing annuity. Such a transaction would not, however, be a transfer of the existing annuity. It cannot therefore be used to support the treatment of the existing annuity as an available resource. Instead, the Department's position would treat the hypothetical proceeds from the creation of a new annuity as a currently available resource. There is no statutory basis for such a theory and, indeed, adopting it would tend to undermine the MCCA rule that "no income of the community spouse shall be deemed available to the institutional spouse." 42 U.S.C. § 1396r-5(b)(1). Under such a theory, there is no clear limit on the hypothetical transaction proceeds that could be treated assets, whether based on the sale of a future stream of payments tied to a fixed income retirement account, social security, or even a regular paycheck.
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> [James, supra, 547 F.3d at 218-19 (emphasis added).]

The Third Circuit based its decision on 42 U.S.C. § 1382a(a)(2)(B) (the provision of the Supplemental Security Income program that states that annuity payments are income),[2] and 42 U.S.C. § 1396a(a)(10)(C)(III) (which is known as the "single methodology" statute, requiring the Medicaid program to use the same income and resource methodology as the Supplemental Security Income program), and 42 U.S.C. § 1396r-5 (which is a section of the Medicaid Act that by its very terms supersedes all other provisions of the Medicaid Act, 42 U.S.C. § 1396r-5(a)(1)).

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[1] 42 U.S.C. § 1396r-5 was a section of the Medicaid Act added by the Medicare Catastrophic Coverage Act, commonly known as the MCCA. The purpose of the MCCA was to protect the community spouse's income for the community spouse and to add certain income and resource spousal impoverishment provisions to the Medical Act.

[2] See also 20 C.F.R. § 1121(a) and N.J.A.C. 10:71-5.4(a)(3).

In short, based upon these sections, payments from an annuity are income of the community spouse that does not affect the eligibility of the institutionalized spouse. Also, the provisions of the Medicaid Act upon which the holding of the James court is based supersede all other provisions of the Medicaid Act. I FIND that the decision in the James case is binding, valid, and controlling.

By letter dated January 23, 2009, counsel for the plaintiff in this matter provided UCBSS and my office with a copy of the decision in Weatherbee v. Richman, 2009 U.S. Dist. LEXIS 4402 (C.A. No. 07-134 Erie, January 22, 2009). Distinguishing this case from the facts in James, the court in Weatherbee at page 27 stated that:

> I find that the language of 42 U.S.C. § 1396(e)(4), when viewed in the context of the subsection as well as pertinent provisions of the Medicaid Act, is unambiguous and does not support the DPW's reading of it. By its terms, 42 U.S.C. § 1396p(e)(4) expressly limits its effect to "this subsection." It does not purport to alter the well-established rule under the Medicaid Act, contained in 42 U.S.C. § 1396r-5, that "no income of the community spouse shall be deemed available to the institutionalized spouse." 42 U.S.C. § 1396r-5(b)(1). Indeed, 42 U.S.C. § 1396r-5(a)(1) provides that, "[i]n determining the eligibility for medical assistance of an institutionalized spouse . . . the provisions of this section supersede any other provision of this subchapter . . . which is inconsistent with them." In view, 42 U.S.C. § 1396p(e)(4) simply makes clear that which would otherwise be implied. Namely, that disclosing the purchase of an annuity and naming the state as a remainder beneficiary will not, in and of itself, *prevent* a state from denying eligibility for income or resources derived from an annuity. A state could, for example, deny eligibility for a variety of reasons including, but not necessarily limited to, lack of an actuarially sound annuity or where the income from the annuity was not solely for the benefit of the community spouse. Consistent with the "holistic" approach espoused by the courts in the above cases, and having examined 42 U.S.C. § 1396p(e)(4) in context, I conclude that if Congress had intended to "ring the death knell" for otherwise compliant annuities, it would have said so. It did not.
>
> I also find that it would be incongruous for 42 US.C. § 1396p(e)(4) to have the meaning ascribed to it by the DPW.

> As set forth above, Congress delineated earlier in the subsection those additional requirements with which a Medicaid applicant must comply in order to *successfully* transfer assets, without penalty, to an irrevocable annuity. It is unreasonable to assume that Congress would have intended to take with one hand (i.e., through the operation 42 U.S.C. § 1396p(e)(4)) that which it had just given with the other.
>
> Turning now to preemption, Weatherbee contends that the Pennsylvania statute upon which the DPW relies in treating the income from an otherwise compliant annuity as an available resource is inconsistent with the treatment of annuities under the Medicaid Act. I agree.
>
> It is a familiar and well-established principle that the Supremacy Clause invalidates state laws that "interfere with, or are contrary to," Federal law. U.S. Const. Art. VI, cl. 2; See Hillsborough County v. Automated Med. Labs, 471 U.S. 707, 712-13 (1985). A conflict between a state and Federal law arises when "compliance with both federal and state regulations is a physical impossibility," Florida Lime and Avacado Growers v. Paul, 373 U.S. 132, 142-43 (1963), or when state law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," Hines v. Davidowitz, 312 U.S. 52, 67 (1941). As stated in [Lankford v. Sherman, 431 F.3d 496 (8th Cir. 2006]:
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> "While Medicaid is a system of cooperative federalism, the same analysis applies; once the state voluntarily accepts the conditions imposed by Congress, the Supremacy Clause obliges it to comply with federal requirements. See Jackson v. Rapps, 947 F.2d 332, 336 (8th Cir. 1991) (applying conflict preemption doctrine to state AFDC law, analogous to Medicaid's system of cooperative federalism). See also King v. Smith, 392 U.S. 309, 316, 326-27, 88 S. Ct. 2128, 20 L. Ed. 2d 1118 (1968); Planned Parenthood of Houston and Se. Tex. v. Sanchez, 403 F.3d 324, 337 (5th Cir. 2005) ("once a state has accepted Federal funds, it is bound by the strings that accompany them"). Lankford, 451 F.3d at 510."

The resolution of this issue is driven largely by my previous conclusion that Congress did not intend, through the operation of 42 U.S.C. § 1396p(e)(4), to permit the DPW to count the income stream from Weatherbee's annuity as a resource under these circumstances. The decision in James is also instructive. To reiterate, the James court,

as had the district court below, specifically rejected the DPW's contention that income from an annuity could be treated as an available resource because to do so would "tend to undermine the MCCA rule that "no income of the community spouse shall be deemed available to the institutionalized spouse." James, 547 F.3d at 218-219 (quoting 42 U.S.C. § 1396r-5(b)(1)). The Court was clearly concerned that under the "theory" espoused by the DPW, a whole variety of income streams could improperly be treated as countable resources. Id. at 219. That concern is no less present here. Finally, having surveyed the legislative landscape, the Court concluded that the James annuity was not abusive because its purchase was not among the transactions considered "suspicious" by Congress. Ibid. I reach the same conclusion with respect to the Weatherbee annuity.

STANDARD FOR SUMMARY DECISION

Summary decision is available in the administrative court pursuant to N.J.A.C. 1:1-12.5. The regulation provides that summary decision is appropriate if

> the papers and discovery which have been filed, together with the affidavits, if any, show that there is no genuine issue as to any material fact challenged and that the moving party is entitled to prevail as a matter of law. When a motion for summary decision is made and supported, an adverse party in order to prevail must by responding affidavit set forth specific facts showing that there is a genuine issue which can only be determined in an evidentiary proceeding. If the adverse party does not so respond, a summary decision, if appropriate, shall be entered.
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> [N.J.A.C. 1:1-12.5(b).]

The summary decision rule is substantially the same as the summary judgment rule under R. 4:46-2. See Contini v. Bd. of Educ. of Newark, 286 N.J. Super. 106, 121 (App. Div. 1995) (which recognized that the summary decision standard in administrative proceedings is substantially similar to that of New Jersey Court Rule 4:46-2).

The New Jersey Supreme Court in Brill v. Guardian Life Insurance Company, 142 N.J. 520, 540 (1995), stated that a motion judge is required to consider "whether the competent evidential materials presented, when viewed in the light most favorable to the non-moving party, are sufficient to permit a rational fact finder to resolve the alleged disputed issue in favor of the non-moving party." Therefore, where a moving party demonstrates, by competent evidential material, that no genuine and material issue of fact exists, the court must grant the motion for summary judgment. Similarly, the rules governing administrative proceedings provide that summary decision may be granted if there is "no genuine issue of material fact and the moving party is entitled to prevail as a matter of law." Borough of Lincoln Park Bd. of Educ. v. Bd. of Educ. of Boonton, EDU 5944-02, Initial Decision (April 2, 2003), adopted, Comm'r (May 15, 2003), aff'd, St. Bd. (Nov. 5, 2003), <http://lawlibrary.rutgers.edu/oal/search.html>. Under N.J.A.C. 1:1-12.5(b) the determination to grant summary decision should be based on the papers presented as well as any affidavits filed with the application. Ibid. Here the parties jointly requested summary decision.

I **CONCLUDE** that there are no genuine issues of material fact, and in accordance with the decision in the above-referenced James and the Weatherbee cases, the petitioner's resources do not exceed the permissible limit for Medicaid eligibility.

ORDER

Accordingly, Summary Decision is granted and it is **ORDERED** that the decision of the UCBSS denying Medicaid eligibility to E.F. be and is hereby **REVERSED**.

I hereby **FILE** my initial decision with the **DIRECTOR OF THE DIVISION OF MEDICAL ASSISTANCE AND HEALTH SERVICES** for consideration.

This recommended decision may be adopted, modified or rejected by the **DIRECTOR OF THE DIVISION OF MEDICAL ASSISTANCE AND HEALTH SERVICES**, the designee of the Commissioner of the Department of Human Services, who by law is authorized to make a final decision in this matter. If the Director of the Division of Medical Assistance and Health Services does not adopt, modify or reject this decision within forty-five days and unless such time limit is otherwise extended, this recommended decision shall become a final decision in accordance with N.J.S.A. 52:14B-10.

Within seven days from the date on which this recommended decision was mailed to the parties, any party may file written exceptions with the **DIRECTOR OF THE DIVISION OF MEDICAL ASSISTANCE AND HEALTH SERVICES, Mail Code #3, P.O. Box 712, Trenton, New Jersey 08625-0712**, marked "Attention: Exceptions." A copy of any exceptions must be sent to the judge and to the other parties.

2-26-09
DATE

Walter M Braswell
WALTER M. BRASWELL, ALJ

Date Received at Agency: 2-26-2009

Mailed to Parties:
Laura Sanders
DIRECTOR AND
CHIEF ADMINISTRATIVE LAW JUDGE

FEB 27 2009
DATE

OFFICE OF ADMINISTRATIVE LAW

ljb