Economic Impact Analysis
Virginia Department of Planning and Budget

12 VAC 30-40 –Eligibility Conditions and Requirements
Department of Medical Assistance Services
February 22, 2005

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 2.2-4007.G of the Administrative Process Act and Executive Order Number 21 (02). Section 2.2-4007.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

The proposed regulations will no longer allow the sheltering of assets using annuities with a balloon payment when determining Medicaid eligibility.

Estimated Economic Impact

In order to qualify for Medicaid benefits, an applicant's income and resources must be below certain thresholds. The federal Medicaid rules allow disregarding of annuities as a resource provided that the annuity is a fair market transaction. An annuity is a financial instrument that provides a stream of payments or a one-time payment sometime in the future in exchange for a down payment today. Currently, an annuity is deemed fair market transaction if the expected return on the annuity is actuarially sound, or is commeasure with the statistical life expectancy of the beneficiary. Thus, so long as the return on the annuity over the life expectancy of the beneficiary is actuarially reasonable, applicants can disregard any resources by sheltering them through an annuity transaction.

To illustrate, consider an individual who arranges for an annuity transaction with his heirs and exchanges a $1 million house for a 15-year annuity that pays $1 a year, (or does not pay anything at all) for the next 14 years with an end-point value of $1.5 million (a balloon payment) on the 15th year. Under the current rules, this annuity would be considered actuarially sound provided that the statistical life expectancy of this individual is truly 15 years and the current interest rate is 3%. Because he will receive only $1 per year (or receive nothing) for the next 14 years, he will meet the Medicaid income threshold (unless he has other sources of income). Because the annuity transaction is actuarially sound and he can disregard the value of the annuity, he will also meet the Medicaid resource eligibility criteria (unless he has other resources). As a result, this individual will qualify for Medicaid benefits for the next 14 years, at which time he may enter into another annuity transaction to maintain his eligibility longer. This loophole that exist under the current regulations defies the purpose of the Medicaid program, which is to provide health benefits to those who cannot afford them.

The Department of Medical Assistance Services (the department) has noticed a growing number of applicants, consistent with national trends[1], taking advantage of the current loophole especially with the intent of qualifying for Medicaid long-term care services. The eligibility workers reported about 15 cases in the last year with questionable annuity transactions, but nonetheless had to approve eligibility under current regulatory language. There were probably many other cases not reported to the department as these types of transactions are allowed under the current rules. Even though a precise estimate of the number of cases with questionable annuity transactions is not available, the fiscal burden that each case puts on the Commonwealth is significant. For example, it costs about $72,000 per year to provide nursing home care to a recipient and another $4,695 to provide other Medicaid services. If the average length of time spent in a nursing home is about two to three years, the total cost per case becomes about $153,390 to $230,085. Then, for the 15 cases the department were notified last year the total cost could be about $2.3 million to $3.4 million. Because the 15 cases is probably a gross under estimate, the actual costs of the loophole could be much higher.

The proposed regulations will prevent individuals from impoverishing themselves in order to qualify for Medicaid benefits using annuity transactions. The proposed regulations will consider an annuity an available resource and allow disregarding of annuities from the resource test under certain conditions. One of the conditions is that the annuity provide equal monthly installments. This will effectively prevent annuities with a balloon payment being used to qualify for Medicaid because the equal payments will be subject to income criteria. Another condition is that the annuity names the Commonwealth as the beneficiary of the funds remaining in the annuity, not to exceed the Medicaid expenses. This provision will enable the Commonwealth to recover its expenses before heirs get their share of the inheritance in the event the individual dies. Third condition is that the annuity be irrevocable. The intent of this condition is to prohibit the individual changing the terms of the annuity so that the beneficiary status of the Commonwealth cannot be removed later. Finally, the annuity must be issued by an insurance company, bank, or other licensed business in order to avoid questionable annuity transactions among the family members, neighbors, or friends. Because of the basic principals of the administrative law that it cannot be retroactive, all cases with questionable annuity transactions that have been and will be approved before these regulations become effective will be grandfathered.

The main benefit of the proposed changes is to restrict the sheltering of assets through purchases of annuities by individuals as a means to impoverish themselves and enable them to qualify for Medicaid. The Commonwealth will realize cost savings, as public funds will not be expended on individuals who can afford to purchase their own long-term care. The Commonwealth will realize approximately one half of the cost savings and the federal government will realize the other half. The actual benefits of these changes will depend on how the expected savings are reallocated. They could be used to provide myriad of other public services or goods, or alternately they could be used to reduce the tax burden. There is no available information as to what will eventually be done with these savings. However, there is no question that the proposed changes will provide the Commonwealth with net economic benefits as the monies are directed to needed services, goods, or used to reduce tax burden. The main costs of this proposal will accrue to those individuals planning to use questionable annuity transactions and take advantage of the existing loophole in the current regulations in order to qualify for Medicaid assistance.

[1] National Association of State Medicaid Directors, October 2003, "The Role of Annuities in Medicaid Financial Planning: A Survey of State Medicaid Agencies."

Businesses and Entities Affected

The proposed regulations will primarily affect the individuals entering into questionable annuity transactions to qualify for free public health care. The department is aware of 15 approved cases in the last year. However, as these transactions are legal under the current language, it is likely that eligibility workers approved many other transactions without notifying the department. Therefore, the actual number of cases is probably much greater than the 15 known cases.

Localities Particularly Affected

The proposed regulations apply throughout the Commonwealth.

Projected Impact on Employment

The proposed regulations' impact on employment depends on many factors that are impossible to predict. For example, the individuals becoming no longer eligible for Medicaid may continue to receive the health care services from their own resources or could stop receiving them. Also, the expected savings may be used to purchase other goods and services or not spent. Thus, the impact on employment could be positive, negative, or insignificant depending on how individuals and state respond to the proposed changes.

Effects on the Use and Value of Private Property

Similarly, the impact on the use and value of private property cannot be estimated with any reasonable degree of accuracy as it depends on responses of individuals and the state to this regulatory change.