IN THE MICHIGAN SUPREME COURT
APPEAL FROM THE COURT OF APPEALS
M. J. KELLY, P.J., and STEPHENS and O'BRIEN, JJ.

ESTATE OF MARY ANN HEGADORN, by
RALPH HEGADORN, Personal Representative
Plaintiff-Appellant,

v

DEPARTMENT OF HUMAN SERVICES
DIRECTOR,
Defendant-Appellee
_____/

SC: 156132
COA: 329508
Livingston CC: 2014-028394-AA

The appeal involves a ruling that a provision of the Constitution, a statute, rule or regulation, or other State governmental action is invalid.

ESTATE OF DOROTHY LOLLAR, by DEBORAH
D TRIM, Personal Representative
Plaintiff-Appellant,

v

DEPARTMENT OF HUMAN SERVICES
DIRECTOR,
Defendant-Appellee
_____/

SC:156133
COA: 329511
LivingstonCC: 2014-028395-AA

ROSELYN FORD,
Plaintiff-Appellant,

v

DEPARTMENT OF HEALTH AND HUMAN SERVICES
DIRECTOR,
Defendant-Appellee
_____/

SC:156134
COA: 331242
Washtenaw CC: 15-000488-AA

BRIEF ON APPEAL - APPELLANTS ESTATE OF MARY ANN HEGADORN, ROSELYN FORD, and THE ESTATE OF DOROTHY LOLLAR

REPLY BRIEF

_____

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TABLE OF CONTENTS

INDEX OF AUTHORITIES

CASES

FEDERAL STATUTES

ADMINISTRATIVE

ARGUMENT

I. THE DEPARTMENT ATTEMPTS TO IMPOSE THE WRONG STATUTORY STANDARDS ON THE APPELLANTS.

The Appellants have correctly outlined the Medicaid application procedure and rules applicable to processing the applications of these applicants, at pages 1-8 of Appellant's principal brief. The Department attempts to interject concepts that do not apply to these applications by citing cases that either have been superceded by later changes in the Medicaid statutes, do not apply to a married applicant, or do not stand for the proposition stated by the Department. For example, the case of *Lewis v Alexander*, 685 F.3d 325 (2012), from the third circuit, (cited at pages 3, 26 and 32 of the Appellee's brief) dealt specifically with certain "special needs trusts" or "supplemental needs trusts" and the validity of a state statute which sought to regulate these types of trusts differently than the federal statute. That case did not deal with married applicants or the interpretation of the meaning of 42 USC 1396a(10)(G) or 42 USC 1396p(d)(3)(B). However, that *Lewis* case did note:

> And the Supreme Court has emphasized the importance of giving full effect to all of Congress' statutory objectives, as well as the specific balance struck among them. See *Rodriguez v. United States*, 480 U.S. 522, 525–26, 107 S.Ct. 1391, 94 L.Ed.2d 533 (1987) ("Deciding what competing values will or will not be sacrificed to the achievement of a particular objective is the very essence of legislative choice and it frustrates rather than effectuates legislative intent simplistically to assume that whatever furthers the statute's primary objective must be the law."). *Lewis* at 343

And, further:

> Even more important is the structure of the asset-counting rules. While Defendants focus on the specific mandate-and-exception structure of 42 U.S.C. § 1396p(d) (3) and (4), both of these sit within a complex and comprehensive system of asset-counting rules. Congress rigorously dictates what assets shall count and what assets shall not count toward Medicaid eligibility. State law obviously plays a role in determining ownership, property rights, and similar matters. Here Congress has

> not only provided a comprehensive system of asset counting rules, it has actually legislated on this precise class of asset. Defendants argue that Congress left a gap or an unprovided-for case with regard to these trusts. But with such a rigorous system, it seems clear that Congress intended to create a purely binary system of classification: either a trust affects Medicaid eligibility or it does not. *Id.* at 343-344

The Department attempts to further cloud the true issues in these cases by claiming that "To qualify for Medicaid benefits, the medically needy must spend-down their assets and income to the levels of the categorically needy where 'any further expenditures for medical expenses then would have to come from funds **required for basic necessities**," and asserts that this "rule" applies to these Appellants who applied for long term care nursing home benefits, citing 42 USC 1396a(a)(10)(C), along with *Davis v Shah*, 821 F3d 231, 238-39 (CA 2, 2016); and *Roach v Morse*, 440 F3d 53, 59 (2006) as the authority. [Appellee's Br., p 7]. However, 42 USC 1396a(a)(10)(C) contains no such statement. *Davis v Shah* was a home-care case involving coverage for orthopedic footwear and compression stockings. *Roach v Morse* involved a challenge to the propriety of certain questions on the Medicaid application used by the state of Vermont. So again, the cases cited by the Department as authority for a standard which it says is applicable to these Appellants, dealt with completely different questions and did not deal with any of the matters relevant to these cases.

The Department also says that the following statement applies to these Appellants: "To qualify for Medicaid benefits, the medically needy must spend-down their assets and income to the levels of the categorically needy where "any further expenditures for medical expenses then would have to come from funds required for basic necessities.'" citing *Atkins v Rivera*, 477 US 154, 158 (1986) as the authority. [Appellee's Br., p 7]. The *Atkins v Rivera* case dealt with Applicants for medical assistance benefits, **who each worked** full-time but did not receive medical benefits from

employers and dealt with the question of whether the methodology provision for determining eligibility used by Massachusetts was permitted by the Medicaid statutes. That case dealt with a different Medicaid statute, 42 USC 1396a(a)(17). It did not deal with the provisions of the Medicaid statutes designed to prevent spousal impoverishment which are at issue in this case, and those provisions did not exist in 1986.

The correct starting point for the Medicaid rules applicable to institutionalized spouses is 42 USC 1396r-5. See Appellant's principal brief, pages 1-5. As outlined at pages 2-4 of Appellant's principal brief, the Michigan BEM [see BEM 400, 401, 402, and 405 included in the Appendix filed with that brief], includes provisions drawn from the federal Medicaid statutes that permit Medicaid applicants such as these Appellants to transfer assets, without penalty, to reduce their countable resources (however, the wording of those BEM's does not exactly correspond to the actual Medicaid statutes). These provisions include various ways for the couple to change the character of an otherwise countable resource to an income stream for the benefit of the community spouse, including use of certain annuities [see 42 USC 1396p(c)(1)(F) and (G)], promissory notes [see 42 USC 1396p(c)(1)(I)], and sole benefit trusts payable to the community spouse [see 42 USC 1396p(c)(2)(B)(i) and (ii)]. In each of these three cases, the Department determined that these sole benefit trusts satisfy the statutory requirements for such trusts, that no "divestment" penalty is applicable, and that payments from those trusts are to be treated as income to the spouse/beneficiary [see Department's trust analysis memo dated 8/29/2014, for the Ford trust (Appx 229a); Department's trust analysis memo dated 8/13/2014, for the Hagadorn trust (Appx 379a); Department's trust analysis memo dated 8/29/2014, for the Lollar trust (Appx 382a). Income payable to the community spouse is not "available" for the institutionalized spouse. See 42 USC

1396r-5(b)(1), and Appellant's principal brief at page 20.

II. THE DEPARTMENT'S INTERPRETATION IS NOT ENTITLED TO MOST RESPECTFUL CONSIDERATION.

The Department claims that its interpretation is entitled to "most respectful consideration" and cites several state of Michigan cases as support (Appellee's Br, p 9). However, those cases do not support the Department's claim. First, all of these cases deal with the administration of State of Michigan legislation, not federal statutes. And, while rule-making has legislative qualities, the power must be exercised pursuant to valid enabling legislation that does not improperly delegate "legislative" authority. [See *Taylor v. Gate Pharmaceuticals*, 468 Mich 1, 10 n 9, 658 NW2d 127 (2003)]. Also, the Department's BEM items, and especially its unpublished interpretative memos, do not come anywhere close to qualifying as state regulations, let alone federal regulations. But even more importantly,

> While [state] administrative agencies have what have been described as "quasi-legislative" powers, such as rulemaking authority, these agencies cannot exercise legislative power by creating law or changing the laws enacted by the Legislature. [*In re Complaint of Rovas Against SBC Michigan*, 482 Mich 90, 98; 754 NW2d 259 (2008)]

As this Court held in *In re Complaint of Rovas Against SBC Michigan*,

> By ignoring the statutory context, the PSC's implicit interpretation of "false" was erroneous. "As a general matter, words and clauses will not be divorced from those which precede and those which follow. When construing a series of terms ... we are guided by the principle that words grouped in a list should be given related meaning." In other words, this Court applies the doctrine of *noscitur a sociis*, which "stands for the principle that a word or phrase is given meaning by its context of setting." [*Id.* citations omitted.]

In the cases at bar, the Department has indeed ignored statutory context to interpret its BEM

contrary to context of the words of the applicable federal statute.

III. 42 USC 1382b(e)(2)(A) IS NOT APPLICABLE TO THIS CASE

The Department continues to erroneously claim that 42 USC 1382b(e)(2)(A) is the applicable statute to use when evaluating a trust for the Medicaid program being administered under 42 USC 1396, in spite of the provisions of 42 USC 1396a(a)(10)(G) that specifically direct the States not to apply that provision to the 42 USC 1396 Medicaid program.

To avoid the directive which Congress included in 42 USC 1396a(a)(10)(G), the Department boldly proclaims that it only applies to the "categorically needy" in spite of the fact that 42 USC 1396a(a)(10)(G) includes no such limitation. (Appellee's Br, pp 17-18). The actual wording of that statute is short and to the point, In particular, 42 USC 1396a(a)(10)(G) reads as follows:

> "A State plan for medical assistance must -
> (10) provide -
> (G)that, in applying eligibility criteria of the supplemental security income program under subchapter XVI for purposes of determining eligibility for medical assistance under the State plan of an individual who is not receiving supplemental security income, **the State will disregard the provisions of subsections (c) and (e) of section 1382b of this title;** (emphasis added).

As can be seen, 42 USC 1396a(a)(10)(G) refers to "A State plan for medical assistance . . ." generally without specifying any particular type of of **medical assistance** and directs the State to "disregard the provisions of subsections (c) and (e) of section 1382b of this title" when ". . . . applying eligibility criteria . . . for . . . determining eligibility for medical assistance". The only limitation is that the individual applicant "is not receiving supplemental security income," a circumstance that does not apply to any of these applicants.

The Department's position that 42 USC 1382b(c) and (e) apply to the facts in this appeal is

belied by the agency's own Medicaid State Plan and its policies governing Michigan's program in the Michigan Bridges Eligibility Manual (BEM), which the Department itself created.

For example, the subject of 42 USC 1382b(c) is "disposal of resources for less than fair market value". Attachment 2.6-A, Page 26 and Supplement 9b to Attachment 2.6-A of Michigan's State Medicaid Plan [attached as Appx 385a, 386a] says that the transfer of assets rules for all groups in Michigan's Medicaid program are governed by Section 1902(a)(18) of the Social Security Act (SSA) [which is 42 USC 1396a(a)(18)] and Section 1917(c) of the SSA [which is 42 USC 1396p(c). Likewise, the Department's BEM Item 405, page 22 [Appx 378a] cites Section 1902(a)(18), [which is 42 USC 1396a(a)(18)] and Section 1917 of the SSA, [which is 42 USC 1396p] as the legal base for the agency's policy governing transfers of resources for less than fair market value. Nowhere do the Department's Medicaid State Plan or its policies governing Michigan's Medicaid program say that transfers of assets for less than fair market value are governed by 42 USC 1382b(c). The subject of 42 USC 1396b(e) is trusts. Attachment 2.6-A, Page 26 of the Michigan State Medicaid Plan [see Appx 385a] states that treatment of trusts for all eligibility groups in Michigan's Medicaid program is governed by Section 1917(d) of the SSA [which is 42 USC 1396p(d) not 42 USC 1382b]. The Department's BEM Item 401 contains its "policy" governing how trusts are treated in Michigan's Medicaid program. Page 18 of that policy [Appx 342a] cites Section 1902(a)(18) of the SSA [which is 42 USC 1396a(a)(18)] and Section 1917 of the SSA [which is 42 USC 1396p] as the legal base for the Department's policy governing trusts. Nowhere does the Department's Medicaid State Plan or its Medicaid policies say that trusts are governed by 42 USC 1382b(e).

Also, perhaps predictably, the Department claims that the POMS SSI Trust rules must be applied to these long term care Medicaid applications, again ignoring the fact that these long term

care Medicaid applications are governed by the provisions of 42 USC 1396 [and in especially, 42 USC 1396a(a)(10)(G)]. The Department justifies this claim on the basis that SSI rules in general are to be applied, but again ignores the specific wording contained in the various sections of 42 USC 1396. (Appellee's Br, pp 25-26). To bootstrap its argument, the Department quotes from the POMS SI 01120.201 trust rules **that are based on** 42 USC **1382b**(e)(3)(B), and which use wording identical to 42 USC 1382b(e)(3)(B). (See Appellee's Br. pp 24-27). The Department then goes on to assert that "SSI policy standards for long-term care regard all the assets in the claimants' Trusts as countable for Medicaid eligibility" (*Id* at 26) even though those POMS do not apply to long term care Medicaid. The POMS SI 01120.201 itself cites "Social Security Act as amended, Section 1613(e)" [which is 42 USC 1382b, and includes 42 USC 1382b(e)(3)(B)] as the authority for that POMS. [see Appx 391a], which rules 42 USC 1396a(a)(10)(G) says the State is **not** to use.

Even without the directive contained in 42 USC 1396a(a)(10)(G), the Department's assertion that 42 USC 1396p(d)(3)(B) includes the applicant's spouse cannot be sustained under applicable statutory analysis rules. See Part III of Appellants' principal brief, pps 22-34.

IV. THE DEPARTMENT ACKNOWLEDGES THAT ONLY THE SPOUSE IS A BENEFICIARY OF THESE SOLE BENEFIT TRUSTS.

The Department acknowledges that in each of these cases, the couple transferred assets into a trust which "guaranteed that distributions from the trust could be made only to that community spouse and that all trust assets would be paid out to him within his expected life time." (Appellee's Br., p 5). And further, that these provisions qualified these trusts as "'Solely for the Benefit of" Trusts (SBO Trusts), which ensure that **the beneficiary is the only one who can benefit from the trust**." (*Id;* emphasis added). Therefore, the Department has acknowledged that no one other than

the spouse of the applicant can benefit from these trusts. This result corresponds exactly to the criteria established by Congress for this type of trusts - to benefit the spouse of the Medicaid applicant. Congress did not impose any particular dollar value limitation on the amount that can be "funded" into this type of trust. And, Congress also did not impose the "any circumstances test" of 42 USC 1396p(d)(3)(B) on trusts that do not include the Medicaid applicant as a beneficiary. (See Appellant's principal brief, Part III, pages 22-30.)

V. APPELLANTS QUALIFIED AS OF THE DATE OF FILING OF THE APPLICATIONS.

The Department acknowledges that 42 USC 1396r-5 applies to these applications, (Appellee's Br., p 12), but then claims that 42 USC 1396r-5 somehow changes the analysis of the requirement that an "asset" must be "available" to be a countable "resource". But, 42 USC 1396r-5 does not address the definition of "resource" and indeed says that it does not do so. (Appellant's principal brief, p 32).

As we have shown above, and also as shown by Appellant's principal brief, the state may consider **only** such income and assets as are "available" to the applicant **at the time the application is filed**, as determined by the federal rules, which means that if a property right cannot be liquidated, the property will not be considered a resource of the individual (or spouse). (See 20 CFR 416.1201(a); and Appellant's principal brief, pages 18-21).

The Department's brief, at page 12, tries to mischaracterize the timing of when the assets of the spouses are to be evaluated for availability, by equating the "time of institutionalization" with the timing of "the eligibility determination". Such mischaracterization violates the statute.

The Department is required to determine the amount of "resources" of the institutionalized

spouse **at the time of the filing of the application for Medicaid benefits**, not whenever it gets around to deciding to process the application. 42 USC 1396r–5(c)(2). Also, according to the Department's own BEM, asset eligibility exists when the asset group's countable assets are less than, or equal to, the applicable asset limit at least one day during the month being tested." See BEM 400, page 6, Appx 263a.

The Department acknowledges (at page 20 of its brief) that neither the Ford trust nor the Lollar trust permitted distributions from those trusts at the time those Medicaid applications were filed. But the Department then claims (also at page 20 of its brief) that the fact it delayed the processing of the Ford Medicaid application allows it to ignore the distribution restrictions applicable to that trust at the time the Ford Medicaid application was filed. The Department cannot change the application date by delaying the processing of the application, which it unquestionably did in Ford.

The Department then claims (also at page 20 of its brief) that "The Hegadorn Trust never had any limitations on timing of distributions, and the entire trust corpus could have been distributed to the beneficiary at any time". However, that is not true, because the Hegadorn Sole Benefit Trust included a distribution schedule which calls for distributions of $3,717.00 per month (See Appx 211a), and both before or after qualification, during any month in which an institutionalized spouse is in the institution (subject to exceptions not applicable to this analysis), "no income of the community spouse shall be deemed available to the institutionalized spouse". 42 USC 1396r–5(b)(1). This is the same result that applies to annuity payments to the spouse of the applicant.

Therefore, whether or not the Sole Benefit Trusts at issue in these cases would call for a distribution to the spouse within a few months after the Medicaid applications were filed, or even the next month, would not affect the amount of "resources" that are to be counted, or not counted,

for the month in which the application was made. The Department has acknowledged that for the Lollar and Ford trusts, initial payment from each trust was delayed to a time after the month of application. Appellee's brief, pages 5, 20. The Department has also acknowledged that distributions from these trusts are deemed to be "income" of the recipient [See page 3 of this brief] .

Since the determination of the amount of countable resources for an initial eligibility determination is to made "as of the time of application for benefits" (see 42 USC 1396r–5(c)(2), cited above), none of the assets of any of these trusts was an available "resource" to the applicant or the applicant's spouse. [see Appellant's principal brief, page 21].

RESPECTFULLY SUBMITTED,

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