DHA-15 (R10/97)

STATE OF WISCONSIN
Division of Hearings and Appeals

In the Matter of

[redacted]

DECISION

MDV-51/36122

PRELIMINARY RECITALS

Pursuant to a petition filed August 21, 1998, under Wis Stat. § 49 45(5), to review a decision by the Racine County Dept of Human Services in regards to Medical Assistance (MA), a hearing was held on September 23, 1998 at Racine, Wisconsin. At the request of the petitioner, the record was held open for 30 days for the submission of additional information.

The issue for determination is whether the county agency correctly denied the petitioner's application for MA due to a divestment of assets.

There appeared at that time and place the following persons.

PARTIES IN INTEREST:

Petitioner

[redacted]

By Timothy Crawford, Attorney
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EXAMINER
Kenneth D. Duren, Attorney
Division of Hearings and Appeals

FINDINGS OF FACT

1 Petitioner (SSN/ [redacted], CARES # [redacted], is a resident of Racine County

2 On May 29th and/or May 30th, 1998, the petitioner executed six unsecured Promissory Notes, one each to each of six adult children, in identical amounts of $9,166 Each note provided by their

respective terms that _____ as"Holder", would convey $9,166 to each child, as "Maker(s)", and each of the six children agreed to repay the sum transferred in $68 75 per month installments, under each of the Notes. These payments were to continue every month, until final payment of the remaining balance due, on February 21, 2011. The payment schedule included payment of interest at the rate 9% per annum. Each Promissory Note stated that it was non-negotiable and non-assignable; and that all obligation to make payments under any respective Note was cancelled and extinguished upon the death of the Holder as if paid in full at that time See, Exhibits #2-#7.

3. The petitioner .became an institutionalized resident of a Racine County skilled nursing facility on or about June 5, 1998; she applied for MA at the Racine County agency on July 8, 1998.

4. On August 7, 1998, the county agency issued a manual Positive Notice informing the petitioner that her application for MA card services was approved, effective June 5, 1998, and that her request for services other than MA card services, (i e.,,institutional-MA) was denied due to her divestment of $54,996. The notice also informed, _____ that the divestment caused a penalty period during which she would be ineligible running from May, 1998, through July, 1999 Finally, the notice informed _____ that , "If this creates a situation of "undue hardship" (a serious impairment to the institutionalized person's immediate health please feel free to contact me." See, Exhibits #1A & #1B

5. The petitioner filed an appeal with the Division of Hearings & Appeals on August 21, 1998

DISCUSSION

In a Fair Hearing such as this, the petitioner has the burden of proof to establish his or her eligibility for Medical Assistance and that the divestment determination and denial actions taken by the county agency were improper given the facts of the case The burden of going forward then shifts to the county to rebut the petitioner's case and establish facts sufficient to overcome his or her evidence of an incorrect action

A divestment occurs when an institutionalized individual, his spouse, or another person acting on his behalf, transfers assets for less than fair market value, on or after the individual's "look-back date " Wis Stat § 49 453(2)(a). The "look-back date" is defined as 36 months before, or with respect to trusts, 60 months before, the first date the individual is both institutionalized and an MA applicant. Ibid., (1)(f)

If such a transfer occurs, the individual is ineligible for MA for nursing home services for a number of months determined by totaling the value of all assets transferred during the look-back period and dividing that amount by the average monthly cost to a private patient of nursing facility services at the time of the MA application Ibid., (3)(b) The ineligibility period begins with the month of the first divesting transfer of assets Ibid., (3)(a)

A parallel divestment definition is found at Wis Admin Code § HFS 103 065(4). and states in the parts relevant here, as follows

> (4) DIVESTMENT. (a) *Divestment resulting in ineligibility* An institutionalized individual or someone acting on behalf of that individual who disposes of resources at less than fair market value within 30 months . immediately before or at any time after the date the individual applies for MA while institutionalized, shall be determined to have divested

(Emphasis added).

Petitioner executed 6 virtually identical Promissory Notes, as "Holder", whereby she loaned $9,166 to each of her 6 adult children, separately as individual "Maker(s)", on May 29th or 30th,1998 She

subsequently entered an institution and applied for institutional MA The terms of each of the six loans were as described in FF #2, above Petitioner's expert witness testified that, in his opinion, the value of each note received by petitioner was $9,166, and thus no assets were divested for less than fair market value.

After the hearing, the petitioner's attorney submitted a legal memorandum argument raising six different arguments in support of his opinion that the transfer of the cash assets via Promissory Notes did not bar MA eligibility. I turn now to these arguments.

Argument #1: Treat the Installment Note As An Annuity

The petitioner asserts that these Promissory Notes have many of the features of an annuity, and thus should be so treated under the so-called "Annuity Methodology" under MA Program rules.

For purposes of divestment treatment, the Wisconsin Administrative Code states as follows:

> "Annuity" means a written contract under which, in return for payment of a premium or premiums, an individual or individuals have the right to receive fixed, periodic payments for life or up to a fixed point in time

Wis. Admin Code § HFS 103 065(3)(a).

In an annuity, the person making the premium payments *has the right only to the periodic payments* subsequently made to him or her. Upon payment of the premium, all right and interest in the principal investment, i.e , the premium paid, has been conveyed.

> Its determining characteristic is that the **annuitant** has an interest only in the payments themselves and not in any principal fund or source from which they may be derived

See, Law Dictionary, Barron's Educational Series, Inc , by Steven H. Gifis, © (1975), at p 12 See also, Ballentine's Law Dictionary, 3rd Ed , Lawyer's Cooperative, by William S Anderson, ©(1969), at p 77, which states, in the parts relevant here, as follows

> **Annuity.** In the older sense of the term, a yearly payment of a certain sum of money granted to another in fee, for life, or for years In the modern sense, a right, bequeathed, donated, or purchased, to receive fixed or certain periodical payments, without contingency, either perpetually or for life or a stated period of time, *but not including any interest of the annuitant in the principal fund or source from which the payments derive, his interest being only in the payments themselves*

(Italics added.)

In an annuity, the contract itself conveys all interest the payor (usually the annuitant) has in the premiums to the servicing entity, (usually an insurance company) in return for the right to receive the agreed upon periodic payments under the terms of the contract The interest in the principal sum paid is relinquished by the annuitant or payor under the terms of the contract itself

Conversely, in a promissory note, a maker (promisor) receives funds from a holder (promisee) which he or she promises to repay according to terms of time, number of periodic installments, and interest to be paid. Promissory notes often, as here, provide default terms requiring the immediate payment of all sums due from the maker upon contingent events occurring, like failure to make payment and notice of default, declaration of insolvency, and assignment of the note for the benefit of creditors See, Exhibits #2 - #7

The argument proffered here by the petitioner's attorney that these Notes, despite their obvious denomination as "Promissory Notes" are actually "annuities" which do not divest funds for less that fair market value fails for several reasons.

First, even if I were to view them in the light most favorable to the petitioner, these notes are not "irrevocable" annuities contemplated under the provisions of the Wisconsin Administrative Code concerning the divestment treatment of annuities

The purchase of an irrevocable annuity after October 1, 1993, is a divestment if the amount transferred to the annuity exceeds the expected value of the benefit. Wis. Admin. Code § HFS 103 065(4)(at). See also, Wis. Stat. § 49.453(4)(b);Adm Code; MA Handbook, Appendix 14.11.0. The "expected value of the benefit" is defined as "... the amount that an *irrevocable* annuity will pay to a primary annuitant or to joint annuitants during his or her expected lifetime." (Italics added), See, Wis. Admin. Code § HFS 103 065(3)(c); see also, Wis. Stat. § 49.453(1)(c). See also MA Handbook, Appendix 14 11.0.

The terms of the Notes, however, are not "irrevocable", they are quite revocable upon the occurrence of any of the contingent events listed above See, Exhibits #2 - #7. Upon such occurrence, the terms of the Notes call for immediate repayment of the remaining balance of the principal and accrued interest to the holder-promisee, at the option of the holder, under the terms of the contract itself. For example, the petitioner's witnesses [redacted] testified that two of the makers had yet to make any payments on their respective Notes as of the hearing date (September 23, 1998), i.e , 85 days after the first due date under the terms of their Notes. No action has been taken by the holder, however, to give notice of default and/or to accelerate payment of the balance due The option to do so is wholly within his power under the terms of the Notes

"Irrevocable" annuity is nowhere defined in the Code provision or the statute The word has a common legal meaning, in the parts relevant here, as follows·

> **irrevocable.** Not revocable at the will of one party Re Zimmerman, 236 NY 15, 139 NE 764
>
> The usual meaning of the word is never to be revoked, never to be abrogated, annulled, or withdrawn.

Ballentine's Law Dictionary, 3rd Ed., Lawyer's Cooperative, by William S Anderson, ©(1969), at p 668

Implicit in the statutory construction of Wis Stat § 49 453(4), is the understanding that an annuity which is revocable is available to a MA applicant/recipient. The Promissory Notes, at best, constitute revocable annuities. However, given the undeniable fact that the primary characteristic of an annuity is that the annuitant/payor conveys all interest in the principal, and the primary characteristic of a promissory note is that the holder/promisee retains all right to recover the principal plus interest, over time, I conclude that the Promissory Notes at issue here are not annuities at all They are, simply, promissory notes agreeing to repay money principal, with interest, over time

As such, they are not entitled to treatment as annuities under Wis Stat § 49.453(4) or Wis Admin Code § HFS 103 065(4)(at).

Argument #2 Treat the Installment Notes as if they have fmv of Face Value

Prior cases before DHA involving Promissory Notes and divestment have been concerned, among other things, with forgiveness of the debt upon death of the holder, coupled with a large "balloon" payment due

at a distant time on the original conveyance of cash after completion of a nominal or minimal periodic payment schedule The latter troublesome feature is not present in these Notes Rather, these notes provide for regular, uniform, and periodic payments which would result in payment of most if not all of the principal and interest by the due date of February 21, 2011, unless the holder dies The former feature is present here In the event of death, all subsequent sums are "extinguished" under the terms of the respective Notes. This type of note has sometimes been referred to as a "self-canceling installment note", or "skin".

These Notes all indicate on their faces that they are each "NON-NEGOTIABLE" and 'NON-ASSIGNABLE".

The petitioner's attorney argues that all the Notes have a fair market value (*fmv*) at the time of execution of their respective face amounts. Petitioner contends that each Note represents fair market value for the $9,166 conveyed to each of the petitioner's maker relatives He contends, in effect, that any of these Notes could be sold in an arms length transaction on the open market for face value, i.e., $9,166

Attorney Crawford presented Attorney Robert Weber as his expert witness to testify as to the value of the Notes According to Attorney Weber, himself an advocate before this forum of the validity of such "skins" in the MA divestment context in at least one prior case, the 9% interest rate counteracts the admitted downside, the self-canceling aspect, the non-negotiability, and non-assignability Furthermore, he asserts that the non-negotiable, non-assignable language does not prevent the purchase or sale of the Notes themselves, stating that these terms limited only the two parties to the note Upon direct questioning from the examiner as to whether, in his expert opinion, a bank or commerical institution would purchase promissory notes containing such restrictions, he admitted that such financial institutions may not, but the Notes still had value and were "saleable" to someone.

The acceptance of Promissory Notes in exchange for cash is not a divestment if the notes received represent payment at fair market value (*fmv*) for the value of the cash transferred for each Note A Promissory Note can represent *fmv* However, these Notes do not represent *fmv* because of the voluntarily imposed (as opposed to market-imposed) restrictions on their liquidity The petitioner did not have to make these Promissory Notes non-assignable and non-transferable, she chose to do so

The use of these two terms renders these Notes invalid as "negotiable instruments"under the Uniform Commercial Code, as codified in Wisconsin.

> A promise or order other than a check is not an instrument if, at the time that it is issued or first comes into possession of a holder, it contains a conspicuous statement, however expressed, to the effect that the promise or order is not negotiable or is not an instrument governed by this chapter

Wis Stat § 403 104(4)

> "Instrument" means a negotiable instrument

Wis Stat § 403 104(2)

These Notes are non-negotiable instruments As such, they are uneforceable under the terms of the Uniform Commerical Code Without the protections found therein for "holders in due course", transfer to any commercial or financial community purchase is extremely unlikely. Combine with this great deficiency the fact that any subsequent holder might not get repaid if the original holder dies prior to full term, and any tangible "market" for sale of these Notes evaporates Removing potential commercial /financial institutional buyers from the market for the Notes drastically affects both the available pool of potential

buyers in the market and the resultant market value of the Notes. Adding a forgiveness upon death clause renders the prospective purchase of such a restricted and diminished note a veritable crapshoot. *Someone somewhere at some time* might be persuaded to buy such a Note, but to suggest that such a note has anything remotely near face value as fair market value is patently absurd.

Attorney Crawford argues at length that the non-negotiable, non-assignable, features of each Note "...does not take away its fair market value It simply reduces its marketability." Brief, at p.2. He then opines that, "It is ludicrous, ridiculous, and preposterous to say that an Installment Note that is legally enforceable could have no value whatsoever." Ibid., at p. 3.

It is this entire argument which has "no value" whatsoever. This argument is sheer sophistry Mr Crawford urges that the only evidence presented which establishes the correct value is that of his expert. I reject that contention. I find the testimony of Mr. Weber to be self-serving, evasive, uncorroborated by any credible statement of the value of these Notes from any member of the financial community in writing or otherwise, uncorroborated by any meaningful economic, legal, or financial data readily available to a financial or legal expert, and simply not credible.

These Notes are not enforceable under the statutes as negotiable instruments Any potential market for such restrictive and specious paper is hypothetical at best.

I find the county agency's determination of the fair market value (*fmv*) of these non-assignable, non-negotiable, Promissory Notes as $0, to be supported by the preponderance of the credible evidence presented at the hearing. Petitioner has transferred $54,996 to her children without receiving fair market value (*fmv*).

Argument #3: Due Process is Violated

The petitioner's attorney asserted that the county agency did not challenge installment notes as impermissible divestments between January, 1997, and thereafter through March, 1998, and that to do so now violates the constitutional principle of due process of law

It is the long-standing policy of the Work & Family Services Unit of the Division of Hearings & Appeals, formerly known as the Office of Administrative Hearings, that hearing examiners do not possess equitable powers or the authority to render provisions of state law or policy unconstitutional. Rather, this office must limit its review to the law as set forth in statutes, federal regulations, and administrative code provisions See, Wisconsin Socialist Workers 1976 Campaign Committee v.McCann, 433 F Supp 540, 545 (E D Wis.1977)

Argument #4 Policy Provides that these Promissory Notes are Exempt from Divestment Treatment

The petitioner asserts that the Department's own policy provides that " .prior Installment Notes would be grandfathered, and would not be challenged " Petitioner's Argument, at p 4. Attorney Crawford asserts that a proposed policy statement of April 16, 1998, and a policy statement issued on June 9, 1998, both make it clear that the Department intended to grandfather in pre-existing Notes The Notes at issue here show execution dates of May 29th or 30th, 1998 Crawford, somewhat puzzlingly, asserts that these Notes were "entered into prior to April 16, 1998, and thus, should be grandfathered in, and should not constitute a divestment." Petitioner's Argument, at p 4.

This argument is also without merit. First, the proposed policy of April 16, 1998, was never adopted nor effective It was not implemented Second, Attorney Crawford is mistaken as to when these agreements were entered into. These Notes were entered into on May 29th or 30th, 1998, after April 16, 1998, but before June 9, 1998 Third, the Department's policy statement of June 9, 1998, states as follows

> EFFECTIVE DATE This is a *clarification of existing policy* that is effective upon the date of this operations memo – June 9, 1998.

Operations Memo, dated June 9, 1998, at p.2.

However, as the petitioner pointed out at the hearing, the Department rescinded this policy clarification under cover of a letter dated July 22, 1998, written by the Department's Chief of the Medicaid Eligibility Section, Susan Wood. See, Exhibit #8, Letter of Susan Wood, Chief, dated July 22, 1998.

Finally, the practical effect of this policy recision is that the pre-existing policy, which was being clarified, remains enforceable. See, Wis Admin Code § HFS 103 065(4), see also, MA Handbook, App. 14.1.0, et. seq. This policy is not that transferring assets in return for promissory notes is a divestment Rather, the transfer of assets for a promissory note without *fair market value* being returned, is a divestment. See, prior decision in accord, *In re William Chase*, DHA Case No MED-40/#11073(Wis Div. Hearings & Appeals March 20, 1997)(DHFS), at p 3.

The Department's policy is exactly this last point. This argument is without merit

Argument #5: The Amount Divested, if any, is the Difference between What she is Paid Monthly by the Payors Under the Notes and What She Would Be Paid Monthly Under an (Unspecified) Investment with an Insurance Company

First, there is absolutely no meaningful evidence in the record demonstrating what return the petitioner might be paid by an insurance company for a hypothetical investment in an unknown or unspecified instrument.

Second, the comparable itself is inapposite here It assumes that the Notes themselves are effective under their own terms and constituted fair market value. However, as I explained above in the Argument #2 section, I have already determined that the Notes are so specious and non-negotiable as to have no value under the preponderance of the evidence test This argument only grows legs to walk *if* one concludes that the initial transfer of cash-for-notes was for *fmv* I have concluded that it was not

Argument #6: Hardship

The petitioner's attorney makes a generalized argument, without citation to law or recitation of any facts in the record as to Ms. physical condition, that the denial by the county agency of the petitioner's application for MA here would work a "hardship" on her

An individual who has been determined to have made a prohibited divestment will, nevertheless, not be found ineligible for Institutional Medical Assistance if it is shown that the denial or termination of eligibility would work an undue hardship See, Wis Admin Code § HSS 103 065(4)(d)2d. MA Handbook, App 14 4.0.6.

Wis Admin. Code § HFS 103.065(d)2d provides as follows.

> The denial or termination of eligibility would work an undue hardship In this subparagraph, "undue hardship" means that a serious impairment to the institutionalized individual's immediate health status exists

Again, the petitioner's attorney makes an argument for which there was little or no meaningful evidence produced at the hearing While a hearing examiner has the duty to develop the record as fully as possible,

he or she cannot anticipate and develop every defense argument a petitioner desires to make in a subsequent brief. This is especially so when the recipient is represented by counsel The counsel here failed to produce any evidence as to the specific status of the petitioner's physical health No evidence establishes that the denial of MA would mean "*serious*" impairment to her "*immediate*" health In fact, the only evidence as to the petitioner's present condition was to the effect that there was no present reason to believe that the petitioner would die prior to the expiration of her life expectancy, which would expire after the terms of the Notes expired in 2011.

In addition, the county agency advised the petitioner in its two Notices of the availability of MA if a serious physical impairment or hardship existed See, Exhibit #1A & #1B Yet no request or information was provided to the agency.

Finally, the petitioner also mentioned a " hardship" allegation in her petition for review, and yet, as noted above, no tangible evidence was produced at hearing supporting this argument. The petitioner has not met her burden of proof on this point, either.

Conclusion

A divestment occurred here in the amount of $54,996. The problem this case presents was *not* that the transfer of cash was made in return for Promissory Notes This is permitted Rather, this situation is a divestment because the Notes were so restrictive in their terms as to render each of them non-negotiable, non-assignable, and non-enforceable under the Uniform Commercial Code, and more likely than not, worthless The agency action is sustained

CONCLUSIONS OF LAW

The county agency correctly determined that the petitioner divested $54,996, to her six children in return for non-negotiable, non-assignable, and non-enforceable Promissory Notes with no fair market value

NOW, THEREFORE, it is ORDERED

That the petition for review herein be, and the same hereby is, dismissed

REQUEST FOR A NEW HEARING

This is a final fair hearing decision If you think this decision is based on a serious mistake in the facts or the law, you may request a new hearing. You may also ask for a new hearing if you have found new evidence that would change the decision To ask for a new hearing, send a written request to the Division of Hearings and Appeals, P O Box 7875, Madison, WI 53707-7875

Send a copy of your request to the other people named in this decision as "PARTIES IN INTEREST "

Your request must explain what mistake the examiner made and why it is important or you must describe your new evidence and tell why you did not have it at your first hearing If you do not explain these things, your request will have to be denied.

Your request for a new hearing must be received no later than twenty (20) days after the date of this decision. Late requests cannot be granted. The process for asking for a new hearing is in sec 227 49 of the state statutes A copy of the statutes can found at your local library or courthouse

APPEAL TO COURT

You may also appeal this decision to Circuit Court in the county where you live Appeals must be filed no more than thirty (30) days after the date of this hearing decision (or 30 days after a denial of rehearing, if you ask for one).

Appeals for benefits concerning Medical Assistance (MA) must be served on the Wisconsin Department of Health and Family Services, as respondent, P.O. Box 7850, Madison, WI 53707-7850.

The appeal must also be served on the other "PARTIES IN INTEREST" named in this decision. The process for Court appeals is in sec. 227.53 of the statutes.

Given under my hand at the City of Madison, Wisconsin, this 10th day of November, 1998

/Kenneth D Duren

Kenneth D. Duren, Attorney
Division of Hearings and Appeals
119/

cc. Racine County DHS
Susan Wood, DHFS
Attorney Timothy Crawford