STATE OF MICHIGAN

IN THE CIRCUIT COURT FOR THE COUNTY OF GRAND TRAVERSE

IN THE MATTER OF
ELIZABETH A. MARDEN,

Petitioner

File No. 08-26616-AA
HON. PHILIP E. RODGERS, JR.

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Attorney for Petitioner

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DECISION AND ORDER ON APPEAL

On November 9, 2006, the Petitioner's husband passed away. The Petitioner received the following annuity and life insurance payouts as a result of his death:

On June 13, 2007, Bankers Life Annuity in the amount of $28,922.82.

On June 13, 2007, Bankers Life Annuity in the amount of $57,732.79.

On June 27, 2007, Trans American Life in the amount of $1,008.

On June 28, 2007, Trans American Life in the amount of $9,000.

In July, the Petitioner applied to the Department of Human Services ("DHS") for Medicaid long-term care assistance. Her application was denied because she had too much money in her bank accounts.

On August 17, 2007, the Petitioner purchased investment units in the Marden Family, LLC for $111,460.47. The Marden Family, LLC is a limited liability company. According to the company's operating agreement, for two years from the acquisition of the investment units, no investment unit may be sold, assigned, transferred, pledged or otherwise disposed of without approval by a super majority of the voting members. After two years, a member may, without consent, sell the investment units according to the buy-sell provisions of the operating agreement which guarantee compounding 2% yearly interest on the amount paid for the units from the date of purchase to the date of sale.

On September 14, 2007, the Petitioner applied for Medicaid long-term care assistance with a retroactive application to the month of August 2007. On November 29, 2007, a DHS Eligibility Specialist generated a Medical Program Eligibility Notice which stated that the Petitioner's investment in the Marden Family, LLC was a divestment for the purposes of determining Medicaid eligibility and, therefore, Medicaid would not pay for long-term care for the divestment period from August 1, 2007 through February 23, 2009. [1]

The Petitioner requested an administrative hearing which was held on February 12, 2008. The Administrative Law Judge ("ALJ") found that the Petitioner "transferred the life insurance payouts to a Limited Liability Company (LLC), which made the assets unavailable for 2 years. Therefore, the amount transferred is for less than fair market value, which results in a divestment penalty" and "[a]s a result of the transfer, an available asset of cash that could have been used for the claimant's benefit is currently unavailable."

The Petitioner appealed the ALJ's decision to this Court. Counsel for the parties presented their oral arguments on October 13, 2008. The Court will now describe its legal conclusions.

Standard of Review

A final agency decision is subject to court review but it must generally be upheld if it is not contrary to law, is not arbitrary, capricious, or a clear abuse of discretion, and is supported by competent, material and substantial evidence on the whole record. Const 1963, art 6, § 28; MCL 24.306(1)(d). "Substantial evidence is that which a reasonable mind would accept as adequate to support a decision, being more than a mere scintilla, but less than a preponderance of the evidence." *St. Clair Intermediate School Dist v Intermediate Ed Ass'n/Michigan Ed Ass'n*, 218 Mich App 734, 736; 555 NW2d 267 (1996). If there is sufficient evidence, the circuit court may not substitute its judgment for that of the agency, even if the court might have reached a different result. *Black v Dep't of Social Services*, 195 Mich App 27, 30; 489 NW2d 493 (1992). With regard to whether a decision is arbitrary or capricious, the Court in *Romulus v Dep't of Environmental Quality*, 260 Mich App 54, 63-64; 678 NW2d 444 (2003), stated:

[1] A divestment penalty is computed by dividing the uncompensated value of the resource divested ($111,432.47) by the average monthly long-term care costs in Michigan for the applicant's baseline date (2007 = $5,938). The penalty would preclude Ms. Marden from receiving benefits for eighteen (18) months and twenty-three (23) days.

> To determine whether an agency's decision is "arbitrary," the circuit court must determine if it is 'without adequate determining principle [,] . . . fixed or arrived at through an exercise of will or by caprice, without consideration or adjustment with reference to principles, circumstances, or significance, . . . decisive but unreasoned.' *St. Louis v Michigan Underground Storage Tank Financial Assurance Policy Bd*, 215 Mich App 69, 75; 544 NW2d 705 (1996), quoting *Bundo v Walled Lake*, 395 Mich 679, 703 n 17; 238 NW2d 154 (1976), quoting *United States v Carmack*, 329 US 230, 243; 67 S Ct 252; 91 L Ed 209 (1946). "Capricious" has been defined as 'Apt to change suddenly; freakish; whimsical; humorsome.' *St Louis, supra* at 75; 544 NW2d 705, quoting *Bundo, supra* at 703 n 17; 238 NW2d 154, quoting *Carmack, supra* at 243; 67 S Ct 252.

The Issue

Whether the Respondent is Collaterally Estopped from Claiming that Ms. Marden's Purchase of Investment Stock in the Marden Family, LLC was a Penalizing Divestment

The Petitioner contends that the DHS should be collaterally estopped from claiming that investment in this type of family limited liability company is a divestment. The Petitioner relies upon the precedent of two circuit court cases involving similar specially designed limited liability companies. In those cases, the Medicaid applications were initially denied, the denials were affirmed by the ALJ, and the cases were appealed to the 13th and 19th Circuit Courts which upheld the use of the specially designed limited liability companies.[2] DHS did not appeal either of those decisions and subsequently approved the applications for Medicaid benefits.

Collateral Estoppel

Generally, for collateral estoppel to apply three elements must be satisfied: (1) "a question of fact essential to the judgment must have been actually litigated and determined by a valid and final judgment"; (2) "the same parties must have had a full and fair opportunity to litigate the issue"; and (3) "there must be mutuality of estoppel." *Storey v Meijer, Inc*, 431 Mich 368, 373 n 3; 429 NW2d 169 (1988). "[M]utuality of estoppel requires that in order for a party to estop an adversary from relitigating an issue that party must have been a party, or in privy to a party, in the previous action." In other words, "[t]he estoppel is mutual if the one taking advantage of the earlier adjudication would have been bound by it, had it gone against

[2] *In Re Gault*, Grand Traverse County Circuit Court File No. 06-25485-AA and *In Re Esther Olsen*, Manistee County Circuit Court File No. 06-12519-AA, respectively.

him." *Lichon v American Universal Ins Co*, 435 Mich 408, 427; 459 NW2d 288 (1990), quoting *Howell v Vito's Trucking & Excavating Co*, 386 Mich 37, 43; 191 NW2d 313 (1971).

Our Supreme Court has expressly recognized that "lack of mutuality does not always preclude the application of collateral estoppel. There are several well-established exceptions to the mutuality requirement, such as when an indemnitor seeks to assert in its defense a judgment in favor of its indemnitee, or where a master defends by asserting a judgment for a servant." *Lichon, supra* at 428 n 16; 459 NW2d 288. In *Monat v State Farm Ins Co*, 469 Mich 679; 677 NW2d 843 (2004) the Court held that "mutuality is not required where collateral estoppel is asserted defensively and where the plaintiff has already had a full and fair opportunity to litigate the issue."

In the instant case, the Plaintiff is asserting collateral estoppel offensively. The Michigan Supreme Court's decision in *Howell*, supra is, perhaps, the best-known Michigan case that discusses mutuality. In *Howell*, a Vito's Trucking vehicle struck and killed Hattie Howell and injured her daughter Anna Sue Collins, who was also riding in the Howell vehicle. William Howell, Hattie Howell's husband, filed a wrongful death suit in Michigan against Vito's Trucking on behalf of Hattie Howell's estate, himself, and as guardian for their son, James Howell. Before the case went to trial, Collins obtained a judgment in federal court for the injuries she sustained in the accident. This prompted William Howell to move for partial summary disposition, arguing that Vito's Trucking should not be allowed to relitigate its negligence. The trial court denied the motion as it concerned William Howell, but granted it to the extent that Collins might be involved or have interests in the Michigan suit as Hattie Howell's heir. Our Supreme Court reversed the trial court's decision and remanded the case with instructions for the trial court to reconsider whether William Howell, in all his capacities, should have been granted partial summary disposition. The Court also indicated that "[t]he trial court had discretion to apply collateral estoppel against defendant, mutuality not being a controlling factor."

When the *Howell* case reached the Supreme Court, the Court thoroughly reviewed the collateral estoppel doctrine and the mutuality requirement, though often mentioning res judicata. The Court observed that, despite the familial relations and factual connections between the federal suit and the action in Michigan's courts, William Howell in each of his three roles in the suit (representative, individual, and guardian) and Collins were distinct legal

entities. The Court concluded that William Howell was not "bound" in the instant case by the federal court decision, which precluded applying the federal court result concerning the alleged negligence against Vito's Trucking. In other words, William Howell could not use the determination in the federal proceeding to bar Vito's Trucking from challenging its negligence in the state court action. Thus, Howell essentially prohibited nonmutual offensive collateral estoppel.

In *Keywell and Rosenfeld v Bithellthis*, 254 Mich App 300; 657 NW2d 759 (2002), the Court set forth four factors that should be considered when determining whether offensive collateral estoppel applies. First, is the party attempting to rely on the doctrine bound by the earlier decision? Second, are the same legal entities participating in the second action? Third, will application of the doctrine cause a denial of due process or other important rights? And fourth, will applying collateral estoppel play an important role in the proper administration of justice in the future?

In the instant case, the Plaintiff is not bound by the earlier decisions in *Gault* and *Olsen* because the Plaintiff was not a party or privy to a party in either of those cases. Applying collateral estoppel offensively in this case would deny the Defendant the right to challenge whether the Plaintiff, under the specific facts and circumstances of this case, is entitled to a similar outcome. Therefore, the Plaintiff in this case cannot use nonmutual offensive collateral estoppel to preclude the Defendant from arguing that its decision in this case is supported by substantial, material and competent evidence on the whole record and is authorized by law.

This is not to say that under an analogous fact situation, the outcome would be different. Obviously, if there is no material factual difference between this and the *Gault* and *Olsen* cases, the Court will reach the same legal conclusions and render judgment accordingly.

Analysis

In *Gault*, the plaintiff assigned an annuity worth approximately $100,000 to a family limited liability company. In exchange she received 100,000 non-voting investment shares in the company. The company restricted the sale or transfer of the shares for a period of two years and entered into a buy-sell agreement with Mrs. Gault, guaranteeing her the right to sell her shares after the two-year restricted transfer period at a sale price equal to the purchase price, plus 4% accrued interest.

In *Olsen*, the plaintiff purchased $100,000 non-voting investment shares in the Olsen family limited liability company. The company restricted the sale or transfer of the shares for a period of two years after which she could sell her shares at a sales price equal to the purchase price, plus 4% accrued interest.

In the instant case, the plaintiff purchased $100,000 non-voting investment shares in the Marden family limited liability company. The company restricted the sale or transfer of the shares for a period of two years and entered into a buy-sell agreement with Ms. Marden, guaranteeing her the right to sell her shares after the two-year restricted transfer period at a sales price equal to the purchase price, plus 2% accrued interest.

The only factual difference between this case and the *Gault* and *Olsen* cases is that the rate of return on the investment in *Gault* and *Olsen* was 4%, whereas here it is only 2%. However, this lower rate of return does not affect the Court's analysis.

An asset for Medicaid purposes is defined in 46 USC 1396p as "a resource under the Supplemental Security Income program." A "resource" under the SSI program is defined in the policy and procedure manual used by Health and Human Services employees to evaluate claims as "cash and any other personal property, as well as any real property, that an individual (or spouse, if any) owns; has the right, authority, or power to convert to cash (if not already cash); and is not legally restricted from using for his/or her support or maintenance."[3] "Assets of any kind are not resources (i.e., available and countable) if the individual does not have the legal right, authority, or power to liquidate them."[4]

A "divestment" is defined in the DHS Program Eligibility Manual as "a transfer of a resource by a client or his spouse that: (1) is within a specific time (See 'LOOK-BACK PERIOD' below), and (2) is a transfer for 'LESS THAN FAIR MARKET VALUE', and (3) is **not** listed below under 'TRANSFERS THAT ARE NOT DIVESTMENT.'[5] "Less than fair market value" is defined as "the compensation received in return for a resource was worth less than the fair market value of the resource."[6] "Converting an asset from one form to another of

[3] Federal Social Security Administration Program Operation Manual System or POMS SI 01110.100
[4] POMS SI 01110.115
[5] DHS Program Eligibility Manual or PEM 405
[6] Id.

equal value is **not** divestment even if the new asset is exempt."[7] Thus, it is not divestment to convert countable assets into non-countable assets of equal value.

Federal law allows for the purchase of annuities for no other reason than to circumvent the countable asset provisions and qualify for Medicaid long-term care benefits. Deficit Reduction Act of 2005, Public Law 109-171, § 6012. It also allows for an individual to transfer assets to a family member through a promissory note to circumvent the countable asset provisions and to qualify for Medicaid long-term benefits. *Id* at Section 6016. Federal law provides that an applicant can transfer assets to his or her spouse so long as they are for the spouse's benefit. 42 USC Sec 1396p(c)(2)(B)(l). Section 1396p(d)(2)(a)(ii) provides, in pertinent part, that "an individual shall be considered to have established a trust if the assets of the individual were used to form all or part of the corpus of the trust and if the individual or the individual's spouse created the trust. Sec 1396p(3)(B)(l).

In *Mertz v Houstoun*, 155 F Supp 415, 426-427 (ED Pa 2001), the United Sates District Court for the Eastern District of Pennsylvania held that resources may be placed beyond the reach of either spouse, and thus not count for Medicaid eligibility purposes, with the purchase of an actuarially sound commercial annuity for the sole benefit of the community spouse. In *James v Richman*, Docket No. 3:05-CV-2647 (MD Pa 2006), the Court held that even the income stream from a non-assignable annuity, though liquid and having a market value, is not a countable resource for determining eligibility because federal law excludes income of the community spouse from factoring into the institutionalized spouse's Medicaid eligibility. 42 USC Sec 1396r-5(b)(1). So long as the principal or corpus of an irrevocable annuity or trust cannot be reached by the applicant or spouse, the income derived from such an asset cannot be counted as a resource for Medicaid purposes, notwithstanding the income streams' market value in the eyes of a third party. *Mertz*, 155 F Supp at 426. As the Petitioner points out, the law and the program policies and procedures manuals actually provide for this type of estate planning by trusts, the purchase of US savings bonds or other mechanisms.[8]

Just as in *Gault* and *Olsen*, the purchase of stock in the family limited liability company in this case was not, by definition, a "divestment" because the transfer was not "for less than

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[7] Id.

[8] In *Gault*, for example, the petitioner was ultimately able to secure benefits by using a sole beneficiary trust.

fair market value."[9] In fact, the value of the asset did not change - the asset merely took another form - a form that legally made it unavailable and uncountable. Based on the authority cited herein, not only is the value of the stock not countable, but the income stream from that investment is also not countable.

Since there is no material factual difference between this case and the *Gault* and *Olsen* cases, the outcome should be and is the same. The ALJ's decision was contrary to law and must be reversed.[10] The Petitioner is entitled to Medicaid benefits without a divestment penalty.

IT IS SO ORDERED.

HONORABLE PHILIP E. RODGERS, JR.
Circuit Court Judge

Dated: 10/29/08

[9] PEM 405

[10] In light of *Gault*, *Olsen* and now *Marden*, the Court would advise the Respondent to either appeal this Decision or instruct their Eligibility Specialists and the ALJs that investments in family limited liability companies as an estate-planning tool is a legitimate means of circumventing the countable asset provisions of the law and qualifying for Medicaid benefits. Should these cases continue to appear on this Court's docket, without some material factual difference that would justify a different outcome, any defense will be considered frivolous and the Respondent will be sanctioned.