

Liability Set Asides – Why There is a Need for Codification

Jason D. Lazarus, Esq.

For many years personal injury cases have been resolved without consideration of Medicare's secondary payer status even though since 1980 all forms of liability insurance have been primary to Medicare. At settlement, by judgment or through an award, an injury victim would receive damages for future medical that were Medicare covered. However, none of those settlement dollars would be used to pay for future Medicare covered health needs. Instead, the burden would be shifted from the primary payer (liability insurer or Workers' Compensation carrier) to Medicare. Injury victims would routinely provide their Medicare card to providers for injury related care.

These practices began to change in 2001 when Medicare Set Asides (hereinafter "MSA") were officially recognized by CMS for Workers' Compensation cases. Interestingly, around that same time the General Accounting Office was studying the Medicare system and pointed out that Medicare was losing money by paying for care that was covered under the Workers' Compensation system.¹ Accordingly, CMS circulated a memo in 2001 to all its regional offices announcing that compliance with the secondary payer act required claimants to set aside a portion of their settlement for future Medicare covered expenses where the settlement closed out future medical expenses.² The new "set aside" requirement was designed to prevent attempts "to shift liability for the cost of a work-related injury or illness to Medicare."³ Set asides ensure that Medicare does not pay for future medical care that is being compensated by a primary payer by way of a settlement or an award. The procedures and policy for set asides have been developed through subsequent CMS memoranda known as Frequently Asked Questions.

CMS' rationale for creating an MSA is compliance with the Medicare Secondary Payer Act (hereinafter "MSP"). The MSP is a series of statutory provisions⁴ enacted in 1980 as part of the Omnibus Reconciliation Act⁵ with the goal of reducing federal health care costs. The MSP provides that if a primary payer exists, Medicare only pays for medical treatment relating to an injury to the extent that the primary payer does not pay.⁶ The regulations that implement the MSP provide "[s]ection 1862(b)(2)(A)(ii) of the Act precludes Medicare payments for services to the extent that payment has been made or can reasonably be expected to be made promptly under any of the following" (i) Workers' compensation; (ii) Liability insurance; (iii) No-fault insurance.⁷

There are two issues that arise when dealing with the application of the MSP: (1) Medicare payments made prior to the date of settlement (conditional payments) and (2) future Medicare payments for covered services (Medicare set asides). Since Medicare isn't supposed to pay for future medical expenses covered by a liability or Workers' Compensation settlement, judgment or award, CMS recommends that injury victims set aside a sufficient amount to cover future medical expenses that are Medicare covered. CMS' recommended way to protect future Medicare benefit eligibility is establishment of an MSA to pay for injury related care until exhaustion.

The problem is that MSAs are not required by a federal statute even in Workers' Compensation cases where they are commonplace. Instead, CMS has intricate "guidelines" and "FAQs" on their website for nearly every aspect of set asides from submission to administration. There are no such guidelines for liability settlements involving Medicare beneficiaries. Without codification of set asides, there are no clear cut appellate procedures from arbitrary CMS decisions and no definitive rules one can count on as it relates to Medicare set asides. While there is no legal requirement that an MSA be created, the failure to do so may result in Medicare refusing to pay for future medical expenses related to the injury until the entire settlement is exhausted. This creates a difficult situation for Medicare

beneficiary-injury victims and contingent liability for legal practitioners as well as other parties involved in litigation involving physical injuries to Medicare beneficiaries.

Additionally, problems exist and greater costs may be incurred in the settlement of cases involving Medicare beneficiaries due to the lack of uniformity as well as clarity regarding Medicare Set Asides.⁸ The lack of uniformity and clarity comes from the fact that CMS regularly changes its procedures through publishing new memoranda in the form of FAQs which articulate policy. There have been 11 such memos since the original 2001 memo announcing set asides. Submission of a set aside to CMS for review is sometimes a long process which causes extra costs for parties to the litigation. The amount of the set aside does not take into account that the settlement amount may be lower due to other factors in the settlement apart from medicals. Fees are incurred in preparation of an allocation and submittal to CMS. The costs in creating a set aside may ultimately lower what is available to the injury victim to compensate for non-medical damages. Delays in settlement or the inability to settle cases due to the set aside issue is another significant problem that has a large impact on the tort system. The absence of any law or guidelines in the liability context is a tremendous problem. Since guidelines only exist in Workers Compensation cases, those guidelines are frequently applied to liability settlements. However, this creates many problems as Workers' Compensation cases and liability cases are two very different animals.⁹ Thus, codification is vitally important from a systemic and cost perspective for both comp and liability.

Liability Set Asides

As uncertain and lacking in formal protections as is the Workers' Compensation system is regarding Medicare set asides, it pales in comparison to the current state of affairs in liability settlements. The only known formal mention of Medicare Set Asides in liability settlements comes in the form of an answer to a FAQ in an April 2003 CMS memo.¹⁰ CMS stated:

Third party liability insurance proceeds are also primary to Medicare. To the extent that a liability settlement is made that relieves a Workers' Compensation (WC) carrier from any future medical expenses, a CMS approved Workers' Compensation Medicare Set-aside Arrangement (WCMSA) is appropriate. The WCMSA would need sufficient funds to cover future medical expenses incurred once the total third party liability settlement is exhausted. The only exception to establishing a WCMSA would be if it can be documented that the claimant does not require any further WC claim related medical services. A WCMSA is also not recommended if the medical portion of the WC claim remains open, and WC continues to be responsible for related services once the liability settlement is exhausted.¹¹

While the foregoing is not on point as it addresses the question of whether a set aside is necessary when a 3rd party settlement extinguishes a workers' compensation obligation, it is instructive in the sense that it states CMS's position that 3rd party proceeds are primary to Medicare always. However, a plain reading of the MSP can provide that type of information. There have been some recent statements by CMS officials regarding liability set asides during town hall conferences which gives insight into how CMS views liability set asides. These town hall conferences relate to the new Medicare mandatory insurer reporting requirements under the Medicare, Medicaid & SCHIP Extension Act of 2007 ("MMSEA") which requires insurers and self insureds to report settlements with Medicare beneficiaries to CMS.¹² Due to confusion about this law and misinformation that it somehow requires Medicare Set Asides in third party liability settlements; CMS has been forced to address liability Medicare Set Asides during these calls.

In one such call from 2008, Barbara Wright (Acting Director of the Medicare Debt Management division at CMS), said "I don't believe there is a General Counsel Memo that says there are no liability set asides."¹³ She went on to say "we have a very informal, limited process for liability set asides. We don't have the same extensive ones we have for worker's comp." Finally, she reiterated an important admission that "CMS approval of a set aside amount is not required. It is a voluntary process." In a more recent call from September of 2009, Barbara Wright again addressed the issue of liability set

asides by stating “[t]here is not – the same formal process for liability set asides that there is for Workers’ Compensation set asides. However, the underlying statutory obligation is the same.”¹⁴ In the most recent call in October of 2009, Barbara Wright again emphasized that the review process for liability settlements was voluntary and each CMS regional office makes its own decision whether to review or not.¹⁵ When discussing whether a CMS regional office would review or not she indicated that if the regional office believes there are “significant dollars at issue”, they may review a proposed set aside amount for liability.¹⁶ However, she says that the “fact that they decline to review in a particular case does not create any type of safe harbor. So you’re back to an obligation that has existed essentially since 1980.”¹⁷

The most recent version of the Medicare Secondary Payer manual, revised on 3-20-09, was updated with references to set asides in the liability context. In Section 20, which contains definitions, set aside arrangement are defined as follows:

An administrative mechanism used to allocate a portion of a settlement, judgment or award for future medical and/or future prescription drug expenses. A set aside arrangement may be in the form of a Workers’ Compensation Medicare Set-Aside Arrangement (WCMSA), No-Fault Liability Medicare Set-Aside Arrangement (NFSA) or Liability Medicare Set-Aside Arrangement (LMSA).¹⁸

Clearly CMS has intentions to do something as it relates to liability settlements and set asides since this was included in the MSP manual. The question is what and how will guidelines be developed? Will it be similar to Workers’ Compensation? How will the decidedly different issues involved in liability settlements be addressed?

Given all of the foregoing, legal practitioners, Medicare beneficiary-injury victims and insurers are left guessing as to what to do when a liability settlement is achieved. Is a set aside necessary? If so, how do parties determine if they are necessary? Is it only “significant dollars” cases? What rules apply if you do create a set aside? Do we look to the 12 CMS memoranda? What about the differences

between Workers' Compensation cases and liability cases? Will CMS take into account policy limits in a liability case in determining the sufficiency of an allocation? What happens if policy limits are \$50,000 and the future Medicare covered services are \$150,000? Will CMS take into account comparative fault/contributory negligence issues that may reduce recovery? What about statutory or constitutional caps on damages? Can CMS fail to pay for Medicare covered services post liability settlement for the Medicare beneficiary-injury victim if there is no set aside created?

It should be painfully obvious from the foregoing discussion that codification of set asides is imperative. Given the possible loss of Medicare benefits, as threatened by CMS, a Medicare beneficiary has significant risks when it comes to Medicare Set Asides with little or no corresponding legal remedies. Significant delays persist in the Workers' Compensation MSA process which in some instances leads to settlements falling apart.¹⁹ In addition, liability cases brought on behalf of Medicare beneficiaries may decrease due to the possibility of having to put all of the net proceeds into an MSA. As Rick Swedloff put it in his 2008 law review article, it creates a classic situation of "can't settle, can't sue".²⁰ In the context of conditional payments, he said that the "MSP discourages Medicare beneficiaries and their contingency fee attorneys from bringing suit in simple tort disputes."²¹ That statement is all the more profound today in the face of the increasing complexities of conditional payments and the confusion over Medicare Set Aside issues.

Conclusion

CMS has used the MSP as justification to encourage the use of Medicare Set Asides in Workers' Compensation and liability settlements despite the fact that there is no statute or regulation referencing MSAs. All Medicare beneficiary-injury victims have to rely upon for guidance in this area are published CMS internal memoranda and FAQs. This has led to substantial uncertainty; lack of due process for redress of CMS decisions; delays and the potential to discourage meritorious lawsuits.

I believe the ABA put it best that “[b]ecause CMS has been unable to fix the problems, legislation is needed to provide for certainty, predictability, and efficiency to this set-aside process which was mandated by Medicare without statute or regulation referencing MSP set-asides or providing for a CMS settlement review process.” As the ABA pointed out, legislation regarding Medicare Set Asides needs to establish straightforward criteria for when an MSA should be reviewed; create clear cut rules for establishing an MSA and provide certainty along with reducing delays now disrupting the tort system across the country. I would add that there needs to be an meaningful appellate process in place to allow Medicare beneficiary-injury victims to challenge arbitrary decisions in the MSA process. Finally, any legislation needs to address liability settlements and MSAs not just Workers’ Compensation settlements.

From a public policy standpoint, as a society, we don’t want injury victims to double dip by settling their case and then turning to Medicare for health care coverage when part of their recovery was for future medical. Protecting the Medicare trust fund so it is viable into the future requires we insist that primary payers take financial responsibility and not shift the burden to Medicare. This is what the MSP was meant to do and that objective can be accomplished if legislation is properly crafted.

The Medicare Set Aside process is based on policy memorandum as opposed to federally enacted law. Given what is at stake for Medicare beneficiary-injury victims and other parties, codification is essential to properly protect their rights and provide legitimacy to the system. In the end, codification should mean more certainty for the parties and more money recovered for Medicare.

¹ Edward M. Welch, *Medicare and Worker’s Compensation After the 2003 Amendments*, WORKERS’ COMPENSATION POLICY REVIEW, at 5 (March/April 2003).

² Parashar B. Patel, *Medicare Secondary Payer Statute: Medicare Set-Aside Arrangements*, Centers for Medicare and Medicaid Services Memorandum, July 23, 2001.

³ *Id.*

⁴ The provisions of the MSP can be found at Section 1862(b) of the Social Security Act. 42 U.S.C. § 1395y(b)(6) (2007).

⁵ Omnibus Reconciliation Act of 1980, Pub. L. No. 96-499 (Dec. 5, 1980).

⁶ 42 CFR § 411.20(2) Part 411, Subpart B, (2007).

⁷ *Id.*

⁸ Eric J. Oxfeld, *Congress Must Reform Medicare Set Asides*, FLA. UNDERWRITER, May 2006, at S-9.

⁹ *Zinman v. Shalala*, 67 F.3d 841, 846 (9th Cir. 1995). The Zinman court recognized how different Workers' Compensation settlements are from liability. The court pointed out that "[a]pportionment in workers' compensation settlements therefore involves a relatively simple comparison of the total settlement to the measure of damages allowed for individual components of the settlement, pursuant to a prescribed formula. Tort cases, in contrast, involve noneconomic damages not available in workers' compensation cases, and a victim's damages are not determined by an established formula. Apportionment of Medicare's recovery in tort cases would either require a factfinding process to determine actual damages or would place Medicare at the mercy of a victim's or personal injury attorney's estimate of damages."

¹⁰ Thomas Grissom, *Medicare Secondary Payer – Workers' Compensation (WC) Frequently Asked Questions*, Question 19, Centers for Medicare and Medicaid Services Memorandum, April 22, 2003.

¹¹ *Id.* (emphasis added)

¹² Medicare, Medicaid and SCHIP Extension Act of 2007 (P.L. 110-173). This Act was passed by the House on December 19, 2007, and by a voice vote in the Senate on December 18, 2007. It was signed into law by President Bush on December 29, 2007.

¹³ Barbara Wright, MMSEA October 29, 2008 NGHP Transcript at P. 18

¹⁴ Barbara Wright, MMSEA September 30, 2009 NGHP Transcript at P. 25

¹⁵ Barbara Wright, MMSEA October 22, 2009 NGHP Transcript at P. 65

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ Medicare Secondary Payer (MSP) Manual (Rev. 65, 03-20-09).

¹⁹ Eric J. Oxfeld, *National Issues Impacting Workers' Compensation*

²⁰ Rick Swedloff, *Can't Settle, Can't Sue: How Congress Stole Tort Remedies from Medicare Beneficiaries*, 41 AKRON L. REV. 557 (2008).

²¹ *Id.*