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Fact Sheet

IRS Updated Guidance on Home and Community Based Services and Excluding 'Difficulty of Care' Payments from Gross Income

Prepared By: Wayne Turner
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In January 2014, the IRS announced that payments received by in-home, individual care providers under Medicaid Home and Community Based (HCBS) waiver programs can be treated as "difficulty of care" payments and excluded from the care provider's gross income. (*See* IRS Notice 2014–7 Foster care payment, Medicaid waivers, Jan. 21, 2014 (hereinafter "IRS Notice")). However, the IRS Notice fails to address whether payments from non-waiver HCBS programs, such as self-directed HCBS services authorized under a State Plan Amendment (SPA), can likewise be treated as difficulty of care payments.

In a recently updated Q&A (hereinafter "Updated IRS Q&A"), the IRS clarifies that payments from other programs can be treated as difficulty of care payments, depending "on the nature of the payments and the purpose and design of the program." (Updated IRS Q&A, A1). However, neither the IRS Notice nor the Updated IRS Q&A provides a list of specific HCBS non-waiver programs or requirements to qualify as difficulty of care payments.

This NHeLP Fact Sheet describes how the exclusion of income from difficulty of care payments affects Modified Adjusted Gross Income (MAGI) based eligibility determinations for Medicaid, the Children's Health Insurance Program (CHIP), and Marketplace subsidies. It also identifies advocacy strategies to ensure that states fully implement the difficulty of care payment income exclusion for both waiver and qualified non-waiver HCBS programs.

Difficulty of Care Payments in Foster Care

Federal tax law excludes certain kinds of payments made to foster care providers from the care provider's gross income. (*See* 26 U.S.C. § 131). These include "difficulty of care" payments paid by state agencies as compensation for the additional care provided at home for a "qualified foster individual" living with "a physical, mental, or emotional handicap." (Id. at 131(c)(1)(A)(i)). By excluding these payments from gross income, difficulty of care payments essentially become tax free income.

Excluding these payments lowers MAGI for the care provider's household and therefore affects eligibility for Medicaid, CHIP, or Marketplace subsidies determined under MAGI.

Treating HCBS Payments as Difficulty of Care Payments

In the 2014 IRS Notice, the IRS observed that foster care and HCBS programs share a similar design and purpose – to prevent unnecessary and costly institutionalization of individuals who can be better cared for in a home-setting. Accordingly, in January 2014 the IRS announced that it "will treat qualified Medicaid waiver payments as difficulty of care payments under § 131(c)" and would be excluded from the care provider's gross income. (*See* IRS Notice 2014-7).

However, the IRS Notice fails to address whether non-waiver HCBS program payments, including § 1915(i) State Plan Home and Community-Based Services, § 1915(j) Self-Directed Personal Assistance Services under State Plan, and § 1915(k) Community First Choice, can be treated as difficulty of care payments.

Some states interpreted the IRS Notice as limiting the difficulty of care payment exclusion to only § 1915(c) waiver programs. For example, advocates in California were seeing cases where care providers and other household members were denied Medicaid coverage because the state counted non-waiver HCBS program payments as income, and therefore the household income was too high. In California, the state's In-Home Supportive Services (IHSS) Program is provided under a SPA (§ 1915(j)). Had the non-waiver HCBS care provider payments been treated as difficulty of care payments and excluded from total household income, the care provider and other household members would have been eligible for Medicaid.

Applicability to Non-Waiver HCBS Programs

Advocates should work with their state Medicaid agency and Marketplace, as well as appeals entities, to ensure that MAGI-based eligibility determinations properly exclude HCBS difficulty of care payments from total household income.

The IRS Notice and Updated IRS Q&A provide information for care providers and state agencies on how to report difficulty of care payments and relevant IRS tax forms. However, the Updated IRS Q&A provides no further detail on what non-waiver HCBS programs should be treated as difficulty of care payments.

In the absence of further clarification from the IRS, advocates should consult with state agencies to determine when non-waiver HCBS program payments should be treated as difficulty of care payments. Advocates should also consider raising an argument at state fair hearings to exclude such income based on the IRS Notice and Updated IRS Q&A. As noted in the Updated IRS Q&A, such a determination depends "on the nature of the payments and the purpose and design of the program." (Updated IRS Q&A, A1).

Although the IRS Notice and Updated IRS Q&A do not provide a specific list of requirements, the Notice describes the features which foster care difficulty of care payments share in common with HCBS waiver program payments. According to the IRS Notice, these common features serve as the basis of its decision to treat HCBS waiver payments as difficulty of care payments.

If a state's non-waiver HCBS program is similar in purpose and design to HCBS waiver program payments, the non-waiver payments should be treated as difficulty of care payments.

The IRS Notice describes the general features and commonalities of foster care difficulty of care payments and HCBS program payments, summarized as follows:

- Payments are authorized and made by a state entity or political sub-division;
- Payments are to individual care provider for nonmedical support services;
- Payments are for care provided under a plan of care to an eligible individual;
- Payments are for care provided in the individual care provider's home;
- States assess the suitability of the home for fulfilling the eligible individual's plan of care; and
- State enters into a contract or other arrangement with the individual care provider for services provided to the eligible individual. (*See* IRS Notice 2014-7).

The IRS Notice also cites limits established under federal tax law for excluding foster care difficulty of care payments that would also apply to HCBS difficulty of care payments:

- A provider may not exclude payments for the care of more than 10 eligible individuals under age 19, or
- more than five eligible individuals who are age 19 or over. (*See* IRS Notice 2014-7; 26 U.S.C. § 131(d)(2).

The IRS Notice also establishes:

- Care payments are excluded regardless of whether the care provider is related or unrelated to the beneficiary. (*See* IRS Notice 2014-7).

If advocates can demonstrate that non-waiver HCBS program payments share these same characteristics as difficulty of care payments described for HCBS waiver programs, then non-waiver payments should be excludable from the care provider's gross income pursuant to the IRS Notice and Updated IRS Q&A.

When Excluding HCBS Difficulty of Care Payments Results in Coverage Loss

Advocates should note, however, that under the Updated IRS Q&A, care providers must exclude difficulty of care payments from the gross income – it is not optional. (*See* Updated IRS Q&A, A9). Therefore, some care providers and members of their household may fall into the Medicaid coverage gap if the income exclusion puts their total household income below 100% FPL. These individuals do not qualify for Marketplace subsidies and may not qualify for Medicaid if they live in a state that has not yet implemented the ACA's Medicaid expansion.

Conclusion

Advocates should verify that their state Medicaid agencies and Marketplaces are aware of, and implementing the IRS Notice and Updated IRS Q&A. Eligibility systems and manuals may need to be updated to exclude care provider payments made by HCBS waiver program and qualified non-waiver programs from MAGI. Advocates should also encourage state agencies to issue guidance advising eligibility workers and consumer assisters advising them of the change. Additionally, if the state agency or Marketplace improperly calculated household MAGI by including HCBS difficulty of care payments and wrongfully denied eligibility for Medicaid, CHIP, or Marketplace subsidies, advocates should cite to the IRS Notice and Updated IRS Q&A when appealing.