



Health Care Committee *ABI Committee News*

In This Issue

Volume 7, Number 2 / May 2010

- [The Patient Protection and Affordable Care Act and the Health Care and Educational Reconciliation Act of 2010](#)
- [Continued Pressure on Senior Living Market May Put CCRC Entrance Fees at Risk](#)
- [Materials from the Annual Spring Meeting Committee Session](#)

[Continued Pressure on Senior Living Market May Put CCRC Entrance Fees at Risk](#)

by: [George R. Mesires](#)
Ungaretti & Harris LLP; Chicago

The crash in the residential housing market has effected many Americans, but the downturn has had a particularly disruptive effect on many senior citizens, especially those seeking to gain admission to, or currently living in, continuing-care retirement communities (CCRC). CCRCs are a sub-segment of the senior-living market that provide a broad spectrum of housing, social, wellness and health care options to seniors. Most CCRCs are nonprofit entities and often affiliated with churches, fraternal or charitable organizations. CCRCs provide a continuum of care to seniors—including independent living, assisted living, memory care and nursing care—all on one campus. The target markets for CCRCs are generally seniors 75-plus years old who have equity in their homes.

CCRCs are generally based on an entrance-fee model. A senior seeking to gain admission to a CCRC uses the equity from the sale of his or her home to pay the CCRC's entrance fee, which ranges from \$150,000 to \$750,000. The entrance fee does not result in a fee ownership; rather, the senior is granted a license to occupy the premises, usually pursuant to a residency agreement. Typically, the residency agreement between the CCRC and the resident provides for monthly assessments ranging from \$2,000 to \$4,000, depending on the agreed-upon level of service. CCRCs offer different entrance fee refund policies: some are "100 percent guaranteed" refundable, some are contingent on the CCRC finding another resident for the residential unit, while others are only partially refundable. Generally, CCRCs use a portion of the entrance fees to cover operating costs.

The collapse in the housing market has put significant pressure on the entrance-fee model. First, many seniors have not been able to sell their homes, or have realized significantly less equity in their homes. This has resulted in a lower demand for CCRC admissions, and thus lower occupancy rates for CCRCs. Second, because new residents are not being admitted, former residents (or their estates) are not receiving refunds in those cases where refunds are contingent on the CCRC re-licensing the unit. Third, because of the lower occupancy rates, CCRCs are facing operating expense pressure. Fourth, health-care costs continue to rise. Fifth, CCRC campuses that were not completely built-out are finding few financing

[Committee Officers](#)

[Upcoming Events](#)

[Contribute to the Newsletter](#)

[ABI World](#)

[Newsletter Archives](#)

options to complete their development projects. Not surprisingly, such conditions have resulted in a spate of CCRC and other senior living bankruptcies, which will likely continue without a significant housing rebound.^[1]

Of the myriad issues that arise in these cases, one of the most sensitive issues to both residents and CCRC operators is the treatment of the residents' entrance fees in the event of a bankruptcy. Because a resident usually has no fee interest in the CCRC dwelling unit, the resident's claim to its entrance fee is a general unsecured claim. Moreover, a resident will usually be a party to an executory contract—the residency agreement—that is subject to assumption or rejection under § 365(a) of the Bankruptcy Code. The outcome in these circumstances varies—from nearly complete loss of the entrance fee, to an agreement by the debtor to escrow the entrance fees during the pendency of the bankruptcy case.

Generally, like other assets of the debtor, a resident's entrance fee will become property of the estate from which claims will be satisfied.^[2] Indeed, many residency agreements explicitly provide that the entrance fee shall become the property of the CCRC for use in accordance with terms of the residency agreement. Thus, a resident will have a general unsecured claim for its entrance fee, and will be subordinate to the claims of the CCRC's secured creditors. As a result, in some circumstances, the resident will recover just pennies on the dollar. For instance, in *The Covenant at South Hills* case, the purchaser of the CCRC's assets did not assume the residents' executory contracts as part of the asset sale, and hence, the residents were left with general unsecured claims, resulting in a paltry recovery.

However, there are exceptions to the general rule that funds held in a debtor's account become property of the estate. For example, funds transferred by the debtor and held in escrow for the benefit of a party other than the debtor are not property of the estate once the conditions of the escrow are satisfied.^[3] The bankruptcy estate takes the same interest that the debtor had in the subject property as of the commencement of the bankruptcy case. Accordingly, "if the debtor holds bare-legal title without an equitable interest, the estate acquires bare legal title without an equitable interest."^[4] Courts have generally recognized that § 541(d) describes "the classic trust situation," including situations in which the court may impose a constructive trust.^[5]

To protect residents' entrance fees against the claims of a CCRC's general creditors, some CCRCs place a portion of each resident's entrance fee in escrow or trust for the benefit of the individual resident, not to be shared *pro rata* by all residents. If properly instituted, these arrangements may act to protect the residents' investments from the claims of the CCRC's other creditors in the event of bankruptcy. Thus, any money deposited into trust accounts or escrow funds are owned by the resident, not the CCRC. Obviously, issues such as commingling or failure to segregate may disrupt the protective nature of the escrow account or trust.

In the event of a bankruptcy, a CCRC often has difficulty maintaining residents and attracting new ones. The explicit creation of trusts or escrow accounts is an effective device to encourage residents to enroll with the debtor CCRC. For instance, in *Erickson*, entrance fees accounted for a significant portion of the debtors' annual operating budget, and the collection of such amounts was critical to the debtors' ability to reorganize. Thus, the

debtors moved for the entry of an order authorizing the debtors to escrow, during the pendency of the bankruptcy case, all entrance fees received postpetition. The court entered the order, which was subsequently modified to afford the residents greater protections (namely, that residents shall be entitled to refunds of their entrance fees to the extent deposited in an escrow account during the pendency of a bankruptcy case if they elect to leave their respective CCRC, and requiring the escrow agent to return entrance fees in the escrow account to the residents who had made such payments should any transaction involving a debtor result in a closure of a CCRC).

The disparate results reached in these cases underscore the significant risks that seniors face concerning their CCRC entrance fees. With no significant recovery in the housing market in the foreseeable future, the CCRC will continue to experience pressure, keeping CCRC insolvencies—and the uncertainties involving entrance fees—at issue.

1. See, e.g., *First Community Village*, Case No. 10-54533 (Bankr. S.D. Ohio 2010); *In re Erickson Retirement Communities LLC*, Case No. 09-37010 (Bankr. N.D. Tex. 2009); *In re Plaza de Retiro Inc.*, Case No. 09-10994 (Bankr. D. N.M. 2009); *In re Mayslake Village-Plainfield Campus Inc.*, Case No. 09-43338 (Bankr. N.D. Ill. 2009); *The Covenant at South Hills Inc.*, Case No. 09-20121 (Bankr. W.D. Pa. 2009). The author has been involved in several CCRC insolvencies, including the Erickson Retirement Communities and Mayfield Village-Plainfield Campus bankruptcy cases.

2. See 11 U.S.C. § 541(a)(1); see also, e.g., *Fowler v. Shadel*, 400 F.3d 1016, 1018 (7th Cir. 2005).

3. *FDIC v. Knostman*, 996 F.2d 1133, 1142 (7th Cir. 1992).

4. *In re Foos*, 183 B.R. 149, 156 (Bankr. N.D. Ill. 1995) (internal citations omitted).

5. *In re Marrs-Winn Co.*, 103 F.3d 584 (7th Cir. 1996); *In re Kisak*, No. 96-41075, 1998 Bankr. LEXIS 1903 (Bankr. S.D. Ill. Feb. 27, 1998).