

# BOND

## LIFE ESTATE DEEDS AND HOMESTEAD TRUSTS

### Introduction to Medicaid Planning and Your Home

Long-term care is expensive. As of 2020, the average cost of nursing home care in New York is over \$10,000 per month.

Combine the fact that health insurance and Medicare generally don't cover long-term care, and it should be no surprise that more than seven in ten nursing home residents in New York State utilize Medicaid assistance to cover the cost of care.

Unlike other forms of Medicaid assistance, recipients of Medicaid for long-term care in nursing homes have to pay back the amount they receive. The State can even recover from the assets of the recipient's estate after death. This is especially concerning for individuals hoping to leave their home to their loved ones.

Although owning a home (if it's the applicant's primary residence) generally won't affect eligibility to receive Medicaid, the State can recover its costs by placing a lien on the home.

A common strategy to avoid a lien is to transfer title to the home to the applicant's children before applying for assistance.

While this strategy may sound simple, the timing and means of the transfer require careful planning.

### The Timing of Transfer: "Look-Back" and "Penalty Periods"

In New York, if within five years of applying for nursing home Medicaid the applicant transfers an asset (such as his/her home) for less than its fair market value (FMV), the applicant will be ineligible for Medicaid assistance for the duration of what's called a "penalty period."

Penalty Period = Difference between transfer and FMV ÷ Average monthly cost of nursing home care in your region.

Let's say you own a home worth \$250,000 in an area where the average nursing home cost is \$10,078 per month. If you sold the home to your daughter for \$50,000, then apply for nursing home Medicaid two years later, you will be ineligible for Medicaid for the first 19.8 months in the nursing home.

Penalty Period = \$200,000 (difference between sale and FMV) ÷ \$10,078 = 19.8 Months

To avoid the penalty period, any transfer of the home below FMV must take place at least five years before applying for Medicaid.

### The Means of Transfer: Life Estate Deed and Homestead Trust

The rest of this pamphlet discusses how a homeowner can:

- (1) Transfer his or her home to protect it from Medicaid liens; and
- (2) Enjoy as many of the rights in the home he or she had before the transfer as possible.

Most commonly these goals can be accomplished by transferring the home through a "Life Estate Deed" or by placing the home into a "Homestead Trust." Both instruments offer distinct advantages when it comes to Medicaid planning.

### Protecting your home from the cost of Long-Term Care

#### About Bond, Schoeneck & King

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## The Life Estate Deed

### What is it?

A “life estate deed” splits ownership in a home between the giver (the Grantor) of the home and receiver (the Grantee).

The Grantor deeds his or her home to another person but retains the right to continue to live in and use the home for the rest of his or her life. That right is called a “life estate interest.”

When the Grantor dies, the property passes directly to the Grantees outside of probate and free from the Grantor’s creditors. The Grantees’ future right to own the home after the Grantor’s death is called a “remainder interest.”

### Life Estate Deed Examples

- (1) Mom is a widow and owns a home worth \$250,000. She has two adult children, Mike and Molly. She executes a deed retaining a life estate in the home and giving the remainder interest to Mike and Molly. Mom can continue to live-in and use the home for her lifetime. When she dies, Mike and Molly take the home without probate, and free from mom’s creditors.
- (2) Bill transfers his home to his daughter, Brandy, via a life estate deed. Bill and Brandy’s relationship becomes strained, and he learns that Brandy has a gambling problem and owes years of back income taxes. At this point, Bill can’t take back the home and Brandy’s creditors could put a lien on the home.



Life Estate	
Gift Tax	None if Grantor reserves Special Power of Appointment
Estate Tax	Yes
Step-Up in Tax Basis	Yes, if an income interest or Special Power of Appointment is retained
Capital Gains Income Tax	During Life: Yes if property appreciated since purchase (capital gains tax on remainderman’s portion of sales price) At Death: Full step-up in basis at death allowing Grantee to make immediate post death sale free of tax
Medicaid Look Back Period	60 Months (5 years)
Medicaid Penalty Period	Can get reduced penalty period since only remainder interest is transferred
Fees	Less expensive: Cost of deed preparation, consultation and recording (\$800-\$1,200). Note: a qualified appraisal is recommended (\$400-\$500)
Real Estate Exemption	Seniors: Yes Veterans: Yes STAR: Yes, because life estate beneficiaries are deemed owners of the property

### The Homestead Trust

A Homestead Trust is an agreement between a homeowner (the Grantor) and another person (the Trustee), who receives and holds the legal title to the home for the benefit of "Trust Beneficiaries."

In a Homestead Trust, the Grantors name themselves as "Income Beneficiaries," and direct that all income from the trust be used for the benefit of the Income Beneficiaries.

Reserving the right to income is just like reserving a life estate in that it allows the Grantors to use and enjoy their home for life.

The Grantors can select a designated class of recipients (such as "children of the Grantors") to receive the home when the Grantors pass away. The future recipients are called "Remainder Beneficiaries" because they hold the "remainder interest" in the home.

#### Homestead Trust Example:

Example: A married 70-year-old couple in good health has two children. They own a home worth \$300,000 and \$600,000 in other assets. The couple wants to protect their assets from being taken to pay creditors, including long-term care providers, and to avoid the costs associated with probate. So the couple transfers their home into an irrevocable trust and name a trusted child as the Trustee. The Trustee can manage the home and assets during the parents' lifetimes.

When the parents pass away, their home will not be included in their estates for the purpose of calculation of Medicaid assistance or probate. Rather, the trust assets pass to the beneficiaries according to the terms of the Homestead Trust agreement.

Explained: The State can only put a lien on assets that are included in the probate estate when recovering the cost of long-term medical care paid for by Medicaid. The probate estate includes assets owned individually at the time of death. Assets owned in a Homestead Trust are not owned in the individual's name and so they are not subject to Medicaid recovery.

Caution: It is critical to retain a reserve fund to pay for nursing home fees and any potential penalty period caused by the transfer of the home.



Homestead Trust	
Gift Tax	None if Grantor reserves Special Power of Appointment
Estate Tax	Yes
Step-Up in Tax Basis	Yes, if an income interest or Special Power of Appointment is retained
Capital Gains Income Tax	During Life: Maybe none if trust qualifies as a Grantor Trust, as residence is deemed owned by Grantor and gain is subject to (\$250K/\$500K) exemption At Death: Full step-up in tax base at death allowing Grantee to make immediate post death sale free of tax
Medicaid Look Back Period	60 Months (5 years)
Medicaid Penalty Period	May or may not be able to reduce transfer period, DSS only says reduction if residence is the ONLY asset in trust
Legal Fees	More expensive: Cost of trust and deed preparation, consultation and recording (\$2,000-\$5,000). Note: a qualified appraisal is also recommended (\$400-\$500).
Real Estate Exemption	Seniors: Yes, but must retain life estate interest Veterans: Yes, but must retain life estate STAR: Yes, because life estate beneficiaries are deemed owners of the property

## Life Estate Deeds

Pros
Simple to accomplish: no money exchanged, title search, or closings involved.
Protects the Grantor from having to sell the home to pay for long term care.
When the Grantor passes away, the Grantees own the property immediately without any need for probate.
Only the remainder interest is considered an uncompensated transfer for Medicaid purposes. The life estate won't affect eligibility unless the Grantor is receiving rental income or profits.
Capital gains tax advantage if the home is later sold: the Grantor is only responsible for capital gains tax on the share of proceeds from selling the life estate (generally about 50%). Under current law, the Grantor could exclude up to \$500,000 (\$250,000 if single) in capital gains for selling the primary residence.

Cons
Not easily adaptable to changes that take place after the transfer.
The Grantor needs the Grantees' consent to later sell the home.
Although the home is protected from the Grantor's creditors, it is not protected from the Grantees' creditors.
If a Grantee gets divorced, the remainder interest in the house could be considered a marital asset and the ex-spouse could get as much as 1/2 of the remainder interest.
Capital gains tax disadvantage for Grantees when home is sold during Grantor's lifetime. The Grantees take the original cost basis to offset what is considered earned income on the sale. The Grantees won't be able to exclude any portion of the sale from the capital gains tax calculation because the home is not their primary residence.

## Homestead Trusts

Pros
Prevents home from disqualifying Grantor for Medicaid and protects the Grantor from having to sell the home to pay for long-term care.
Only the Trustee is authorized to sell the home.
The Grantor is a Beneficiary of the trust and can reserve a life interest in the home despite transferring the home to the trust.
Any assets put into the trust are not included as part of the Grantor's estate for the calculation of Medicaid assistance and pass outside of the probate estate.
If formed more than five years before applying for Medicaid, the Trustee can sell the home, convert the asset to cash, and the proceeds are completely protected from long-term care costs, nursing homes, and other creditors.

Cons
Homestead Trusts are more complex, take longer to prepare, and may require the involvement of more parties than Life Estate Deeds.
The transfer of the home into the trust must take place at least five years before applying for Medicaid or else the penalty period may apply.
The Grantors may not name themselves as Trustees.
The Grantors may not name themselves as Remainder Beneficiaries or have access to the principal of the trust.
If the home is sold while Grantors are alive, any retained life estate would need to be relinquished prior to sale. This could result in a penalty being assessed by Medicaid if the grantor applies for or has already been approved for benefits.