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## ELDER LAW NEWS UPDATE

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TO: Clients, Friends and Colleagues

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**SUBJECT: USE OF A LIFE ESTATE AS AN ESTATE AND MEDICAID PLANNING TOOL NOT WORTH RISK!**

### **WHAT IS A LIFE ESTATE?**

In order to understand what a life estate is, you must first understand what it is not. Chances are when you purchased your home, you purchased a *fee interest*, which is your absolute right and possession of it. Absolute right and possession includes the right to live in the home for as long as you wish, the right to lease it and receive rental income, the right to leverage it with a mortgage, the right to determine who will inherit it, the right to modify it and the right to sell it.

When you transfer the interest in your home to children by deed, while reserving both your right to live in it for your lifetime and to receive rental income, you have established a *Life Estate* as well as an estate plan. Your children acquired a vested interest in the *remainder*. The real property will be inherited by your children by operation of law. No further deed needs to be prepared. The children also receive a step up in basis, which means that when they sell the property for fair market value, there should be no capital gains to report.

The Life Estate has also been used by medicaid planners to reduce the value of the transfer made (remainder) and thereby reduce the penalty period that medicaid imposes upon a transfer of resources by the medicaid applicant. Further, if five years pass, the *remainder* is not a countable resource by medicaid. The *Life Estate* is exempt.

At first blush, it appears like a perfect plan to simply achieve both estate and medicaid planning goals. But as in all things in life, the devil is in the details.

### **THE DEVIL IS IN THE DETAILS!**

When you transfer your real property to your children, they obtain a vested interest in your home, that has a value not only to them, but to third parties. This property value may become subject to their creditor's liens for non-payment of medical debt, loans, personal injury awards, as well as marital claims upon divorce. Whether parties would prevail in Court is not the issue. You purchased your home, paid your mortgage and had full access to its value and rights before the transfer. Now, perhaps due to no wrong doing by your child, circumstances arise that would cause liens to be filed against your real property. This not only affects your interest but the interest of your other children. Not worth the risk!

As for its use as a medicaid planning tool, I have personally seen time and again, the havoc it reeks. The parent's once secure and medicaid exempt *Life Estate* interest may become *non-exempt* because an emergency arises, the parent can no longer live at home, and the child can neither lease it nor pay household expenses associated with the premises. Financial panic arises as the children are overwhelmed with the emotional, financial and medical demands required to meet the parent's needs. So the house is sold and the parent now has cash; it is payable to medicaid. Worse yet, if liens were paid from that cash, medicaid still requires that you pay the full *Life Estate* value. The planning is lost. Not worth the risk!

### **USE OF THE MEDICAID ASSET PROTECTION TRUST ACHIEVES IT ALL!**

Many of my clients have already benefitted from the use of the Medicaid Asset Protection Trust. Since the home in trust remains a part of the parent's taxable estate and it is not vested in the children: it won't become subject to the interest of children's creditors, it may still be inherited with a step-up in basis (no capital gain) and without probate, the home may be sold during the parent's lifetime without affecting *medicaid eligibility*, the parent still enjoys the *real estate tax and capital gains exemptions* and the home's appreciation continues to be protected. Worth the Planning!

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