Preserving the Primary Residence
The Minefield of Real Estate Transactions in Elder Law Planning

By Linda S. Ershow-Levenberg

Preservation of the family residence for the benefit of the next generation is an important goal for many of our clients. The real trick is balancing their own financial security against the hopes of their heirs.

Conveyances of the Primary Residence: The Legal Issues
Real property is frequently the largest asset in the portfolio of an individual who consults with an attorney about elder law planning. More often than not, this property is the primary residence of the client and other family members. Clients or their children will often ask their attorney whether they should “give the house to the children so that the nursing home does not ever get it.” They ask because their neighbor told them this is what they should do or because one of the children’s friends heard somewhere that you need to do this. There is never a simple answer to the inquiry, for one size does not fit all when it comes to elder law planning.

When your client is asking about a real estate conveyance in the elder law context, you should consider the impact:

- on the elder’s legal right to remain in the home;
on a Medicaid application for either
at-home or institutional services;
• on the income taxes of both trans-
feror and transferee;
• on the elder’s financial and physical
ability to remain in the home;
• on the elder’s estate plan; and
• of present and future liens and
mortgages.

More specifically:

• Which legal rights in the prop-
erty will be lost in the transfer, and
which ones retained? Is there a safer
alternative than an outright transfer,
such as creation of a different form
of ownership?
• Is the conveyance a gift, and if so, of
what value? What will be the Med-
icaid transfer penalty? Is this the
right time to do the transaction? Is
this property interest a countable
resource or an excludable one for
Medicaid purposes? Is this property
interest associated with an income
stream countable for Medicaid
purposes?
• Will any tax benefits be lost, and
will the transferee acquire income
tax obligations such as capital gains
taxes that can be avoided?
• Will the elder’s financial ability to
remain in the home be in jeopardy
due to a shortage of liquid assets
and the loss of the ability to draw
out the equity in the home via such
vehicles as a reverse mortgage?
• Will this transfer disrupt the elder’s
testamentary plan by dispropor-
tionately shifting assets, e.g., to one
person even though the elder wants
a group of people to share the estate
equally?
• Will this transaction cause exist-
ing mortgages to be called? Will it
remove the risk of a future Medi-
icaid lien?

This article presumes that there is
someone with legal authority to transfer
the real estate by gift. If the elder no lon-
ger has the legal capacity to do so, there
must be a valid durable power of attorney
with gifting powers sufficient to accom-
plish the specific transfer in question. If
no power of attorney exists, considera-
tion must be given to seeking legal guardian-
ship and obtaining court authorization to
make the transfer.

Gathering the Facts
When evaluating the pros and cons of a
property transfer in the elder care con-
text, the following data will be important.

• How exactly is the property titled,
and what is its value?
• Are there any liens against the
property?
• Do all of the owners live in the
home?
• What is the age and health of the
property owner (i.e., the elder)?
• What is the total of liquid assets
available to the property owner?
• How do the property owner’s
monthly expenses compare to his or
her monthly income?
• Is there a “caregiver child” in the
home? How long has he or she been
providing care to the parent?
• How soon will long-term care be
needed?
• Is there a sibling living in the home?
Is this person an owner?
• Is there a spouse? Will the spouse
remain in the home?
• Is there an adult disabled child who
will continue to live in the home?
• What is the plan if the property
owner ever needs round-the-clock
care? Will he or she prefer to stay
home or to move into an assisted
living or other facility?
• How reliable and trustworthy are
the homeowner’s relationships with
the children and their spouses? Do
they have any marital, employment,
or creditor problems?
• Does the property provide rental
income on which the elder
depends?

The Impact on the Elder’s Estate Plan
Not infrequently, an elder carefully
explains that his or her desire is for the
house and other property to be divided
equally among the children or some other
group of heirs. Upon examination, how-
ever, it sometimes turns out that the
estate is mostly comprised of nonprobate

Linda S. Ershow-
Levenberg (linda@
finkrosner.com) is
the principal and
managing attorney of
Fink Rosner Ershow-
Levenberg, LLC, and
has been engaged in
ever law practice in
New Jersey since 1995.
She is a past chair of
the New Jersey Bar
Association’s Elder
Law Section and a
current member of the
National Academy of
Elder Law Attorneys
(NAELA). Certified in
ever law since 1999
by the National Elder
Law Foundation, she
is a peer-selected
member of the NAELA
Council of Advanced
Practitioners.
assets, which have somehow ended up disproportionately in the name of one or two members of the group, whether as co-owners or as death beneficiaries. Sometimes this is intentional; the elder may want to leave everything to just a few in the hope that they will “take care of” the others or may want the whole group to divide the assets among themselves after the elder is gone. As often as not, however, the elder simply did not understand that beneficiary designations such as “POD” (pay on death) or “ITF” (in trust for) control the disposition of an asset despite contrary instructions in the will. This is also often the case with respect to joint ownership of real estate. As title is practically conclusive of ownership and transfers between and among the class create gift and estate tax problems of their own, failure to plan carefully and to adjust the probate and nonprobate assets could be creating problems that are perfectly avoidable.

Transfer of real estate to one member of the class may be an exempt transfer for Medicaid purposes. The elder needs to be advised, however, of the potential impact on his or her overall estate plan so that appropriate adjustments can be made.

The Impact on the Elder’s Legal Right to Remain in the Home

It is important to think about whether the elder’s legal right to remain in the home could be in jeopardy if anything happens to the transferee. For example, what would happen if:

- The person who becomes the owner of the house does not live there and has to file for bankruptcy;
- The new owner (with or without a spouse) does not want the elder(s) to stay there any more, or he or she wants to sell;
- The new owner is sued and the interest in the house is attached by creditors;
- The new owner dies and the house passes through the estate to new owners or must be sold to pay inheritance taxes; or
- The new owner gets divorced and must provide property for equitable distribution?

While the full value of the home should be protected for the new owner, outright transfer of the elder’s entire interest in the primary residence could create substantial legal risk. These risks can be reduced by considering such mechanisms as a transfer with a retained life estate. The transferee would be receiving a remainder interest in the property subject to the life estate and, consequently, anyone succeeding to the rights of that remainderman would also have an interest that is subject to the life estate.

In such a case, the property could not be sold during the life tenant’s lifetime without his or her joining in the deed. The life tenant would receive a pro rata share of the proceeds and could apply a capital gains exclusion if the pertinent state or federal statutory criteria are met. Along with having the beneficial use and enjoyment of the property, the life tenant would also retain the legal obligation to pay for repairs, maintenance, taxes, and the like on the property, as well as the right to receive the rents, if any. Benefits such as senior citizen tax abatements, the ability to procure a reverse mortgage loan, and the capital gains exclusion on sale of the primary residence are also retained. However, the remaindermen need to understand that they do not own 100 percent of the property value during the life tenant’s lifetime, even if the life tenant moves out.

The Impact on Medicaid Eligibility

A person can apply for Medicaid to pay for nursing home care or care in the home when the countable, available resources have been reduced to $2,000 plus an allowance for the community spouse called the community spouse resource allowance (CSRA). Medicaid is a joint federal-state program established by the federal government and implemented by the states, which must conform their requirements and procedures to federal requirements (unless they obtain a waiver from the federal government). The primary sources of federal law are:

- 42 U.S.C. § 1396a (Medicaid statute);
- 42 U.S.C. § 1382a (Supplemental Security Income (SSI) statute);
• 42 U.S.C. § 1396p (regarding penalties for transfers of assets), as amended by the Deficit Reduction Act (DRA) of 2005;
• 42 U.S.C. § 1396r-5 (spousal protection provisions);
• The applicable state Medicaid manual (each state promulgates its own set of regulations in its manual); and
• Trust and asset transfer questions governed by Transmittal 64 issued in 1994 by the Health Care Financing Administration (HCFA), now the Centers for Medicare and Medicaid Services (CMS), and post-DRA transmittals.

The transfer of any interest in property for less than fair market consideration, if made within the five years immediately preceding application for Medicaid, will trigger a disqualification period known as a transfer penalty period unless the property was the primary residence and it was transferred to one of a limited category of transferees. The length of the penalty period is based on the value of the assets transferred, and each state’s divisor for this formula is unique. For instance, in New Jersey, a $250,000 gift will cause a 26.2-month-long penalty period. The result of this disqualification is that Medicaid will not pay for the care during the transfer penalty period, regardless of poverty or medical necessity. The penalty period begins to run when the person is in a nursing home or is receiving home and community-based care services, applies for Medicaid, and is “otherwise eligible.”

The House as a Countable or Excludable Resource under the Medicaid Program
As a general rule, all available real property is counted as a resource when applying for Medicaid, to the extent of the individual’s ownership. However, the primary residence is excluded as a resource if it is occupied by the community spouse. If the house is not occupied by such a person, it may be excluded from consideration temporarily—usually for six months—but if the individual cannot return home and continues to require Medicaid benefits, it must be listed for sale at that point. When the home is occupied by non-member family members other than the spouse, the practices of the county welfare agencies vary as to whether the property must be listed for sale. When the property is occupied by a co-owner family member, a sibling with an equity interest, a disabled family member, or a minor child at the time of the Medicaid application, typically there is no requirement that the property be immediately listed for sale. In the case of Medicaid’s home and community-based services (HCBS) waiver programs, of course, the house may be retained by the Medicaid recipient.

If the elder is applying for Medicaid, family members may want to sell the property, but they also may want to consider keeping the property and renting it out, particularly if the elder retains a life estate. The net rental income after expenses, if any, would be counted as part of the Medicaid recipient’s income. The property will generally receive a step-up in basis at the elder’s death, and the life estate will evaporate. In most states, there is no Medicaid lien against the property if all the elder held at death was a life estate that extinguished at death.

The fact that the property may be excludable under certain circumstances, such as when a spouse lives in the home, does not mean that the home can necessarily be transferred by the elder to someone else without incurring a transfer penalty.

Medicaid Transfer Penalties
Because possession of the real property creates the risk that it will have to be sold to pay for care, elders may want to transfer that property in order to protect it for their heirs or co-owners. Transfer of the complete interest in real property as a gift within the five years preceding a Medicaid application generally causes a lengthy transfer penalty period. If partial interests are transferred, pro rata values are assigned to the amount of the transfer penalty. In a transfer with a retained life estate, actuarial tables published by the Social Security Administration dictate the value of the transfer.
The question then becomes, if the elder transfers the house by gift and later needs round-the-clock care or nursing home care, will there be a way to pay for the care privately during the transfer penalty period until he or she can be eligible for Medicaid? Currently, nursing home care costs between $8,000 and $11,000 per month, and costs for 24/7 care in one’s own home are not much less. The new owner of the house is certainly at liberty to sell, mortgage, or give back the property to pay for the care, but certainly has no legal obligation to do so.

Some Transfers Cause No Penalties

There are some exceptions to the transfer penalty rules with respect to gifts of the primary residence. The primary residence can be transferred to the following categories of recipients without incurring any transfer penalty at all: the spouse, a child under age 21, a child of any age who is blind or permanently disabled, a sibling who has resided in the home for one year or more and already has an equity interest in the home, and a caregiver child (not a grandchild or other relation) who has resided in the home and provided essential and substantial caregiving for two years or more just prior to institutionalization. Transfers of any real property to a trust for the “sole benefit of” the spouse or a disabled individual under age 65 can also qualify as exempt transfers as long as all of the criteria of the regulations are satisfied.

For a married couple, it is generally advisable to transfer the residence to the community spouse. If the community spouse later sells the property, he or she will be able to retain all of the proceeds of sale.

Timing is very important when considering transfers to a caregiver child. Transfer of the property to a caregiver child at the time of institutionalization is an exempt transfer; transfer of that property at a time unrelated to an application for Medicaid will likely cause a period of disqualification that will begin to run after the individual is already in the facility and has applied for Medicaid. Thus, if there is a caregiver child living in the home, the elder should avoid transferring the house prematurely, as he or she could be incurring a transfer penalty that could be avoided if the transfer does not take place until “the last minute.”

The Impact on the Elder’s Financial and Physical Ability to Remain in the Home

Preserving the Ability to Remain at Home through a Reverse Mortgage

For elders of nominal means, the equity in their homes may represent the only “bank account” they have, should they need to make capital improvements, install equipment such as lifts or ramps, or hire a caregiver to live with them at home. A “reverse mortgage” may be available to elderly homeowners to enable them to draw down up to 75 percent of the equity in their homes on a periodic basis. The loan is not paid back until the homeowner either moves out or dies. At that point, the home is sold and the loan repaid.

These loans can be particularly important to elders who have no immediate family and are trying to remain in the community. The older the homeowner, the greater the amount of loan available.

Some elders may require care in the home and may qualify for one of the state’s Medicaid HCBS waiver programs, which may only provide 25 to 40 hours a week of care. Each state has different waiver programs for its HCBS. The elder can draw down the equity via a reverse mortgage to pay for the rest of the needed care. It should be understood, though, that transferring the primary residence eliminates the option of accessing the equity in the home in this manner and also could result in loss of other benefits such as real estate tax exemptions for veterans or the aged. Reverse mortgages may seem expensive, but they are often the only way to free up cash to arrange for round-the-clock care in the home. They can enable an elder to stay home for several years.

More specifically, reverse mortgages are non-recourse loans available to homeowners who are age 62 or older and who live in their own homes. All owners must reside in the home and must be age 62 or older. The youngest owner’s age is used as the measuring life.

Reverse mortgages are more beneficial to the applicant the older he or she...
is. The loan provides a pool of equity that can be drawn out in various ways over time. The value of the property, age of the owner, and current interest rate all affect the usefulness of these products. One major benefit, though, is that there is no need to repay any portion of the loan until the elder dies or vacates the property. Further, if the property increases in value after the pool of equity is tapped out, it is possible to refinance the reverse mortgage and free up equity. This may not occur as often nowadays as it did seven to 10 years ago, but it remains an option. The loan must be in first position, so at the closing, existing liens must be paid off. A portion of the reverse mortgage proceeds can be used for this purpose.

If the elder lives in a house that he or she previously transferred to a revocable living trust, a reverse mortgage is still obtainable. However, if the property was previously conveyed to an irrevocable trust for the benefit of a third party, such as a child, wherein the elder is grantor of the trust but just an occupant of the property, a reverse mortgage will not be obtainable. If the elder has only a life estate, the remaindermen will have to consent to the mortgage. The equity made available will be either limited to the percentage value of the life estate or the entire value if the remaindermen agree to that.

If the elder chooses the option of a line of credit or monthly deposits, these proceeds are not “income” for Medicaid eligibility purposes, and they do not affect eligibility for other programs either.

As with a family loan (see below), if the homeowner is also receiving HCBS under Medicaid, it is advisable to use the reverse mortgage proceeds either in the form of checks paid to third parties (such as the caregiver) or in an amount that can all be spent in the month it is received. Otherwise there is the risk that excess proceeds build up in the account, which could become disqualifying “excess resources.”

The loan must be paid back when the elder dies or vacates the home for six months with no likelihood of return. The property would then be listed for sale. As noted above, Medicaid has a lien against the estate in most circumstances. The reverse mortgage lien would be in primary position before the Medicaid lien.

If the elder dies and the property is bequeathed to someone under the will, this lien will need to be satisfied before that conveyance can be done. Finally, if the elder wishes to transfer the property to, e.g., a caregiver child, this lien would have to be paid off and the child may need to refinance the debt by a new mortgage in his or her own name.

**Preserving the Home by Transferring It to a Trust**

Under certain circumstances, the elder may want to totally relinquish ownership for Medicaid’s purposes but not transfer the home directly to the other parties. The property can be transferred to a trust in which the elder and the trustee sign a use-and-occupancy agreement that entitles the elder to reside there if he or she fulfills certain obligations such as paying rent or expenses in lieu of rent. This arrangement is distinguished from a life estate, for if the trust sells the property, all the proceeds remain in the trust. If the arrangement meets the requirements for grantor trust treatment under Internal Revenue Code (IRC) §§ 671–79 (income tax), the capital gains exclusion for sale of the primary residence will be retained. If it meets the requirements under IRC §§ 2035–41 (estate tax) and the property is not sold during the grantor’s life, the property will be included in the grantor’s estate at death for estate tax purposes and will achieve a step-up in basis to the extent allowed by law.

**HELOCs and Family Loans: Additional Options**

The elder who wishes to remain in the home has additional options that are the same as those that may be used if he or she retains the home at the time residence in a nursing home becomes necessary. These are home equity loans and family loans as described below. Note that the funds drawn from a home equity line of credit (HELOC) or funds lent by a family member are not “income” under the Medicaid rules, so receipt of such payment would not generally put the elder “over the income cap” that certain states have for their HCBS
Medicaid program. However, to avoid any buildup of cash in the Medicaid recipient’s account, payments should be paid directly to a third-party vendor (such as the tax assessor).

**Financing the Costs of the House**

*When the Homeowner Is in a Nursing Home*

When an elderly homeowner goes into a nursing home, he or she does not “sign over the house.” Furthermore, the state does not “take the house.” However, if the house is not being sold, there are carrying costs to be paid: taxes, insurance, water/sewer, lawn maintenance, and utilities. Generally, the house must be listed for sale when a person in a nursing home applies for Medicaid. While it is on the market, it is an unavailable asset.

If the elder has insufficient cash to pay for all of these expenses, there are several options.

**Rent the Property**

The elder can rent the property and charge a fair market rental value sufficient to cover these expenses. If it is rented, the net income above expenses is included in the income that the Medicaid recipient has to pay over to the facility each month. If it is still owned at death, there will be a Medicaid lien against the estate/property.

**Obtain a HELOC**

Write the checks directly to the third-party vendor, caregiver, or tax assessor. If there is a preexisting open HELOC, the elder can use that credit line to pay these expenses. The funds drawn from the HELOC are not “income” under the Medicaid rules, so they can be paid directly to the third-party vendor (or tax assessor). However, if the elder is on Medicaid, he or she cannot use the income to make monthly payments to the bank on the line of credit.

If there is no preexisting HELOC, it is rarely feasible to obtain even a small mortgage or home equity loan to provide cash to carry these costs because underwriting is income-based, and the typical elderly applicant is on a limited fixed income. If the elder needs to apply for a HELOC, he or she will likely need to have a third-party guarantor, such as a child. This may not always be feasible, especially if the child has a lot of debt of his or her own or a poor credit rating. Further, some lenders will not accept a guarantor who is not a partial owner of the real estate. Conveying a partial ownership interest to the child in order to satisfy the lender will raise the specter of a disqualifying gift if a Medicaid application is filed within five years. If the applicant can prove that the conveyance was done exclusively to enable the applicant to obtain a HELOC, the applicant may be able to defeat the presumptive penalty period.

**Obtain Loans from Family Members on an Ongoing Basis**

A helpful family member may be able to lend money to the elder for any of these purposes. In these cases, prepare a conventional mortgage and mortgage note, with a starting balance that reflects the initial amount lent and an elastic clause indicating that the amount due will include “such other documented amounts that the lender has lent to the borrower after the date of execution of this note.” The mortgage, of course, gets recorded with the county clerk. The loans to the elder are not “income” under the Medicaid rules. If the elder lacks legal capacity, make sure that the durable power of attorney authorizes loans. If it doesn’t, guardianship could be necessary.

At the closing of sale of the property, this mortgage can be paid off, and the remaining funds will be distributed to the seller-elder. Payment of this kind of mortgage will not be treated as a “gift” under Medicaid as long as the entire amount can be validated by receipts and verifications.

**Conclusion**

There are many opportunities to preserve the home for the family and safeguard the security of the elder. This article provides general principles, but state laws do vary and a specific evaluation of your particular state’s Medicaid and real estate laws will be critical for your clients.