PRESERVING THE HOMESTEAD:

MEDICAID, TAX AND TITLE ISSUES TO CONSIDER WHEN DRAFTING A DEED OR TRUST

New York State Bar Association
Continuing Legal Education Program
"Advanced Document Drafting for the Elder Law Practitioner"
June 2005

Prepared & Presented by:

MICHAEL J. AMORUSO, ESQ.
Amoruso & Amoruso, LLP
2975 Westchester Avenue, Ste. 207
Purchase, New York 10577
Telephone: 914.253.9255

Web Site: www.amorusolaw.com
www.eldercare-estateplanning.com (Coming Soon!)

INTRODUCTION

Increasingly, clients turn to the Elder Law practitioner in fear that their eventual need for long term care will result in the loss of the asset treasured by them the most, the family home. After all, this is the *sacred asset* - the asset that they worked hard over the years to payoff, where they built the family bond, or the asset that provides our elderly clients with a sense of self and independence. Prior to drafting any instrument to transfer and protect the family home, the Elder Law practitioner must be mindful of the client's emotional connection to the home and their planning objectives in order to recommend the most appropriate asset preservation vehicle.

In particular, certain clients may not be comfortable with utilizing a planning vehicle which causes them to lose control over the home, subject it to the claims of their children's creditors, does not permit them to change beneficial enjoyment of the property or does not guarantee their right to reside in the home. The Elder Law practitioner must balance these concerns with the competing tax, Medicaid and title issues that will certainly result from a transfer of the home. A failure to consider the ramifications of these competing interests potentially may have a devastating financial and emotional impact on the client and/or their beneficiaries and undermine the client's planning objectives. Equally important, however, is the need for the Elder Law practitioner to keep the home preservation plan simple enough for the client to understand, yet sophisticated enough to achieve the desired Medicaid and tax benefits to be gained by a sound plan.

This article will identify and address some of the issues for the Elder Law practitioner to consider when drafting deeds to protect the family home. In particular, this article will explore

the tax, Medicaid and title issues involved with drafting that must be addressed through solid drafting.[1]

I. Exposure of the Family Home – the Medicaid lien and the right of recovery.

Prior to advising a client or drafting a transfer document to preserve the home, the Elder Law practitioner must be cognizant of the risks that the client is seeking to avoid namely, the Medicaid lien and Medicaid's right of recovery.

A. The Medicaid Lien.

The New York State Department of Health through the Medicaid Program (hereinafter "Medicaid") has the right to impose a lien on real property for Medicaid correctly paid[2] (or to be paid) on the Medicaid applicant's or recipient's ("A/R") behalf who is a permanently institutionalized individual and who is not reasonably expected to be discharged from the medical institution and return home.[3] The standard to determine whether or not an A/R is reasonably expected to return home is based upon the A/R's subjective intent and not an objective expectation.[4] In the event that the A/R is discharged from the medical facility and returns to the homestead, the Medicaid lien will dissolve.[5]

It is important to note, however, that Medicaid cannot place a lien on the A/R's real property, even if permanently institutionalized, if any of the following individuals lawfully reside in the same (1) the spouse of the A/R;[6] (2) a child of the A/R who is under the age of twenty-one (21) years or is blind or permanently and totally disabled,[7] or (3) a sibling of the A/R who owns an equity interest in the home and who was residing in the home for at least one year immediately before the A/R's admission into the medical institution.[8]

1. How Medicaid establishes a lien on real property.

At the time the A/R who owns real property files a Medicaid application the agency is required to provide an "Informational Notice to Institutionalized Individuals with Real Property" ("Information Notice") which alerts the A/R that Medicaid may impose a lien against the real property if (1) Medicaid determines that the A/R is not reasonably expected to return home, and (2) none of the exempt persons listed above reside in the home.[9] The Informational Notice also alerts the A/R that a lien will not be placed on the home if the A/R provides medical evidence within twenty (20) days of the application interview date (or later date if undue hardship) to establish that the A/R is reasonably expected to return home.[10] The notice also states that any lien filed against the property will be discharged if the A/R returns home.[11]

> ***PRACTICE POINTER*****:** If a client owns a home and enters a nursing home without an exempt individual living in the home have the client execute an affidavit expressing the temporary nature of their stay in the facility and their intent to return to occupy the home and submit the same with the Medicaid application. (A sample form is attached.) This will evidence the subjective intent to return home and prevent the immediate imposition of a lien against the home. In addition, it will cause the home to retain its exempt status as a homestead for Medicaid eligibility. In the event that the client does not have legal capacity, consider an affidavit from the client's attorney-in-fact, spouse or caretaker indicating client's intent to return home along with adequate medical evidence that the A/R is expected to return home.

It is important to note, however, that prior to filing a lien against the home the agency must afford the A/R the opportunity to transfer the home to any of the following:

1. A/R's spouse;
2. a child of the A/R who is certified blind, disabled, or under the age of 21;
3. a sibling of the individual who has an equity interest in the home and who was residing in the home for at least one year immediately prior to the date the A/R became institutionalized;
4. a child of the A/R who was residing in the in the home for at least two years immediately prior to the date the A/R became institutionalized and who provided care, as defined in 18 NYCRR 311.4(a)(1), to the A/R which permitted the A/R to reside at home rather than in the facility.[12]

If the A/R elects to transfer the home to one of the individuals listed above, the agency must document the intent to transfer and permit the A/R a reasonable timeframe to consummate the transfer.[13] Medicaid views ninety (90) days or longer, if due to difficulty beyond the control of the A/R, as a reasonable timeframe.[14]

After Medicaid approval, the A/R will receive a "Notice of Intent to Impose a Lien on Real Property."[15] If a client receives such a notice it should not be ignored because the client only has sixty (60) days from the date of the notice to appeal the decision to impose the lien.[16] Finally, Medicaid will file a "Notice of Medical Assistance Lien" with the County Clerk's Office.[17] This is the actual Medicaid lien.

2. Treatment of a Life Estate

A life estate is a limited interest in real property where the owner of the interest only has the right to use the property for life (or shorter period), and at the life tenant's death, the property transfers by operation of law to a remainder person. Medicaid is not permitted to file a lien against an A/R's life estate.[18] In addition, a life estate is *not* a countable resource for Medicaid eligibility.[19] These principles apply whether a life estate is reserved in the family home or in other realty.[20]

B. The Medicaid Right of Recovery.

A successful plan to preserve the family home is not complete unless the transfer of the home is shielded from the Medicaid lien and a recovery action from Medicaid. Generally, Medicaid may only recover for benefits correctly paid from:

a. the sale of real property subject to a Medicaid lien of an A/R who was permanently institutionalized during the A/R's lifetime or from the A/R's estate;[21]

b. the estate of the A/R who was fifty-five (55) years of age or older when the A/R received Medicaid.[22]

c. a legally responsible relative (such as a spouse) of sufficient ability to be responsible for dependent's care.[23]

d. Personal Injury claims.[24]

e. A mandatory or discretionary beneficial income and/or principal interest in an Intervivos Trust of an A/R or A/R's spouse.[25]

***DRAFTING TIP*:** If a trust that makes distribution of trust principal subject to the sole discretion of the trustee is the preferred vehicle of the Elder Law practitioner, it is critical that the document preclude the right of invasion by a court to force the exercise of discretion. Consider the following language, "Under no circumstances, however, shall trust principal be subject to any court directed invasion pursuant to the provisions of section 7-1.6 of the Estates Powers and Trusts Law or any other laws of New York or any other state."

1. Legally Responsible Relative

Typically, cases in which Medicaid seeks a recovery from a legally responsible relative of sufficient ability are spousal refusal cases. In the institutionalized spousal context, a legally responsible spouse (i.e., the community spouse) is deemed to have sufficient ability to be responsible for the dependent's institutional care where such spouse has assets greater than $74,820 or $95,100 and/or monthly income greater than $2,378. For community Medicaid (i.e., not nursing home cases), generally, the legally responsible spouse is deemed to have sufficient ability to pay for the dependent's care with resources greater then $5,850 and/or monthly income greater than $975.[26] Where an A/R is receiving Medicaid and there is a legally responsible spouse with sufficient ability to pay, an implied contract is created between Medicaid and the legally responsible spouse that costs may be recovered from such spouse during lifetime *or* from the spouse's estate at death.[27]

In the event that the A/R's spouse does not have a sufficient ability to pay at the time the A/R receives benefits, then the Elder Law practitioner should pursue a defense on this ground to

recovery from the A/R spouse's estate.[28] In addition, Medicaid cannot seek recovery from the A/R's estate during the lifetime of the A/R's spouse.[29]

2. Other defenses to recovery from A/R's estate

It is important to note that the term "estate" is defined by Social Services Law as "all real and personal property and other assets included within the individual's estate *and* passing under the terms of a valid will or by intestacy."[30] Thus, the A/R's estate (and estate of a legally responsible relative) only consists of property in the individual's *probate* estate.[31] There are certain other circumstances, however, where a recovery from the A/R's estate either is not permitted or must be held in abeyance. In particular, Medicaid cannot seek recovery from the A/R's estate if the A/R is survived by:

a. A child under the age of twenty-one (21);[32]
b. A certified blind or permanently and totally disabled child of any age;[33]
c. A sibling with an equity interest in the home and who was residing in the home for at least one year immediately prior to the date the A/R became institutionalized and continues to lawfully reside in the home;[34]
d. a child of the A/R who was residing in the in the home for at least two years immediately prior to the date the A/R became institutionalized and who provided care, as defined in 18 NYCRR 311.4(a)(1), to the A/R which permitted the A/R to reside at home rather than in the facility and such child continues to lawfully reside in the home.[35]

Remember, a lien cannot be placed on the family home until the A/R is given the opportunity to transfer the property to one of the above listed individuals or the spouse.[36] If the A/R fails to make such a transfer then the lien may be place on the family home, however, if any of the above listed exceptions to recovery apply, then Medicaid cannot recover until the exception ceases to exist (i.e., the caretaker child moves out of the home or the home is sold).

Social Services Law also provides a waiver of recovery in the case of undue hardship.[37] In particular, Medicaid has determined that undue hardship may exist if[38]:

a. the estate asset is the sole income-producing asset of the beneficiaries (i.e., family farm or family business) and income produced is limited;
b. the estate asset is a home of modest value (i.e., value no more than 50% of average selling price for county where home located) and is the principal residence of the beneficiary; or
c. other compelling circumstances demonstrating undue hardship.

It must be noted, however, that Medicaid will not find undue hardship if the sole basis is for the beneficiary to maintain a pre-existing lifestyle or if the alleged hardship is caused by estate planning or divesture of assets through Medicaid planning.[39]

3. New York State Partnership Policyholders

For those A/R's who planned ahead and purchased a New York State long-term care partnership insurance policy ("Partnership Policy") which provided the A/R with three (3) years of nursing home benefits or its equivalent, Medicaid cannot impose a lien or seek recovery from the A/R's assets (i.e., the home).[40]

4. Benefits incorrectly paid

There is no prohibition on Medicaid to file a lien on real property or to recover for benefits *improperly* paid if a court judgment is obtained.[41] In such an action, Medicaid only has to prove that benefits were incorrectly paid and not that the improper benefits were procured through an act of the A/R (i.e., fraud, inadvertent omission or latent discovery).[42] With regard to any case that may involve fraud, it is important to remember and advise the client that Medicaid may refer the matter to the district attorneys office for criminal prosecution.

5. Recovery against a Life Estate

Medicaid cannot require an A/R to liquidate a life estate interest.[43] In the event that the A/R sells the life estate interest, the value of the life estate interest is considered an available resource for the A/R's eligibility and is subject to recovery.[44] The value of the life estate interest is determined through the life estate and remainder interest table of the Health Care Financing Administration ("HCFA") in the State Medicaid Manual.[45]

Further, Medicaid cannot force an A/R possessing a life estate interest to rent the property.[46] If the A/R does rent the property, however, any net rental income is counted in determining eligibility if the A/R is required to pay taxes and maintenance on the property.[47] The gross rental income will be considered available for the A/R's care if the A/R is not responsible for paying the taxes and maintenance on the property.[48]

> ***PRACTICE POINTER*****:** Given that Medicaid can place a lien on real property of the A/R and can recover from the estate of the A/R or the A/R's spouse's estate (excluding certain circumstances listed above), the Elder Law practitioner should consider certain transfer vehicles that will remove the asset from both estates. However, consideration must be given to and the client must be advised of the Medicaid, tax, and title issues that will result from such a transfer.

II. Preserving the Home – Medicaid Transfer Issues

It is not atypical for a client or an inexperienced Elder Law practitioner to view their desire to preserve the family home from a potential Medicaid recovery as a simple proposition – deed the property outright to the children. While the logic may appear to have reason, such a maneuver may be a classic example of the "tail wagging the dog" and fail to accomplish the client's objective. For instance, if a sixty (60) year old client, after hearing a sound bite at the coffee shop that someone "lost their home to the nursing home at age 82", retains counsel to transfer a fee interest in her home to her child only to learn two years later that a new civil judgment was filed against her child, did the client (or the attorney) accomplish the objective or

was a future *potential* creditor (Medicaid) merely substituted by another creditor (the child's current judgment creditor).

Alternatively, consider the situation for a married couple where the wife is stricken with a stroke leaving her partially paralyzed and the husband hears from a well intentioned hospital staffer to "immediately get the house out of their names" before applying for Medicaid to cover a rehabilitation stay in a nursing home. The husband goes to a real estate lawyer and has a deed filed transferring the house from both he and his wife to their two children. Three months later the husband is surprised by a large nursing home bill because his wife's Medicaid application was denied due to the transfer of the home.

Unfortunately, these simplistic examples are not uncommon problems that the Elder Law practitioner is called upon to correct. In the context of asset preservation planning, each client's unique circumstances (i.e., health, family relations, finances, and living arrangements) must be carefully considered prior to implementing any strategy to protect the home because the solution for a client in immediate need of Medicaid may be far different than the individual who may need Medicaid in the future.

A. Medicaid Transfer Penalties.

Medicaid is entitled to lookback three (3) years from the first day of the month of application to identify direct transfers and five (5) years for trust related transfers. The purpose of the lookback is to see if the A/R divested themselves of otherwise available assets to pay for their care in order to qualify for Medicaid. Generally, whenever an A/R makes an uncompensated transfer of property (a gift) a time period of ineligibility ("Penalty Period") for Medicaid institutional coverage (i.e., nursing home or Lombardi Program coverage) is created. There is no Penalty Period for community Medicaid eligibility.

The Penalty Period is calculated by dividing the value of the transferred property by the average monthly costs of nursing home care in the A/R's geographic region.[49] In 2005, the rates are as follows:[50]

Region	Counties	Rate
New York City	Bronx, Kings, New York, Queens & Richmond	$8,870
Long Island	Nassau & Suffolk	$9,612
Northern Metropolitan	Westchester, Dutchess, Orange, Putnam, Rockland, Sullivan & Ulster	$8,332
Western	Alleghany, Cattaraugus, Chautauqua, Erie, Genesee, Niagara, Orleans & Wyoming	$6,181
Northeastern	Albany, Clinton, Columbia, Delaware, Essex, Franklin, Fulton, Greene, Hamilton, Montgomery, Otsego, Rensselaer, Saratoga, Schenectady, Schoharie, Warren & Washington	$6,501
Rochester	Chemung, Livingston, Monroe, Ontario, Schuyler, Seneca, Steuben, Wayne & Yates	$6,981
Central	Broome, Cayuga, Chenango, Cortland, Herkimer, Jefferson, Lewis, Madison, Oneida, Onodoga, Oswego, St. Lawrence, Tioga & Tompkins	$5,988

Example 1**:** Ned gifts real property in Albany County to his nephew Bill that has a fair market value of $150,000. A cannot apply for institutional Medicaid for 23.07 months ($150,000/$6501 = 23.07).

1. Transfers to Persons Exempt from Penalty Period

Uncompensated transfers (i.e., gifts) to a "qualified individual"[51] are exempt from the imposition of a Penalty Period. Specifically, a transfer to A/R's

a. spouse;
b. child under the age of twenty-one (21);
c. child who is certified blind or certified disabled of any age;
d. sibling with an equity interest in the home and who was residing in the home for at least one year <u>immediately</u> prior to the date the A/R became institutionalized and continues to lawfully reside in the home;
e. "caretaker child" who was residing in the in the home for at least two years immediately prior to the date the A/R

> became institutionalized <u>and</u> who provided care, as defined in 18 NYCRR 311.4(a)(1), to the A/R which permitted the A/R to reside at home rather than in the facility and such child continues to lawfully reside in the home.

In long-term care crisis planning (i.e., immediate institutional Medicaid is required) a transfer to a qualified individual is an attractive proposition in terms of Medicaid eligibility and recovery. A transfer of the home to any of these individuals, alone, will not cause a Penalty Period for Medicaid eligibility. In addition, as discussed in the Medicaid Recovery section, above, a transfer to a qualified individual, *other* than the spouse, will protect the home from Medicaid recovery. Remember, a transfer of the home to a spouse may insure Medicaid eligibility of the A/R (since there is no Penalty Period for the spousal transfer) and it may protect from the imposition of a lien if the spouse continues to reside in the home, however, if the home remains in the estate of the spouse then it will be subject to Medicaid recovery at the spouse's death. Thus, if an exempt transfer to a spouse is utilized it is imperative that the Elder Law practitioner advise the spouse on post-Medicaid eligibility asset preservation planning to remove the home from the spouse's estate.

It is important to note, however, that a transfer of the home to a qualified individual, without a retained life estate in the A/R may cause a significant capital gains problem upon the sale of the home after the A/R's death if the qualified individual does not satisfy the requirements of IRC § 121 for the capital gains exclusion. If the family plan is to sell the home prior to the death of the A/R, then the reservation of a life estate may be meaningless (from a capital gains perspective for the beneficiary) and the value of the A/R's life estate will be subject to Medicaid recovery upon the sale.

There is often confusion regarding which party (life tenant or remainderperson) may claim the IRC § 121 exclusion upon a sale during the life tenant's lifetime. It should be noted, however, that the IRC §121 capital gains exclusion is *only* available to the life tenant upon a sale of the property.[52] A thorough discussion of preserving the IRC § 121 exclusion for the beneficiaries is set forth below.

III. Preserving the Home – Tax, Medicaid & Title Issues

Planning to preserve the home requires an in depth understanding of the Medicaid right of recovery, Penalty Period and tax ramifications for any suggested transfer. Certain strategies often employed by the Elder Law practitioner to preserve the home include (a) transfers exempt from a Penalty Period to "qualified individuals"; (b) transfers to dependents, either outright or in trust; (c) transfers to dependents retaining a life estate; and (d) transfers to dependents, either outright or in trust, retaining a special power of appointment. Any one of these strategies may not be appropriate for the client due to adverse tax or Medicaid eligibility concerns; thus, it is imperative that the Elder Law practitioner weigh the competing interests of Medicaid eligibility and protecting the home from a Medicaid recovery against the income, estate, gift, and real property tax traps that such transfers will present.

A. Income Tax - IRC § 121 Capital Gains Exclusion.

If there is a possibility that a client may sell the family home prior to death, it is imperative that the planning vehicle used will insure that the client may utilize the capital gains exclusion to offset any gain recognized by the sale of the home. In particular, IRC § 121(a) provides:

> Gross income shall not include gain from the sale or exchange of property if, during the 5-year period ending on the date of the sale

> or exchange, such property has been *owned* and *used* by the taxpayer as the taxpayer's principal residence for periods aggregating 2 years or more.[53]

Unlike the law prior to May 1997 (where individuals over the age of 55 were entitled to a onetime exemption), IRC § 121 applies to *any* individual provided they owned and used the principal residence for an aggregated two (2) year period.[54] Single individuals who meet the criteria are entitled to a capital gains exclusion of $250,000.[55] A married couple who satisfies the ownership and use test and certain additional requirements will receive a $500,000 capital gains exclusion.[56] The IRC § 121 exclusion, however, is only available for the sale of a principal residence once every two (2) years.[57]

> ***Example 2*:** Ned and Sally have continuously resided in their home located in Goshen, New York since they purchased it for $20,000 in 1958. In 2005, Ned and Sally sell their home for $420,000. Since Ned and Sally are married and meet the ownership and use test of IRC § 121, they are entitled to the $500,000 capital gains exclusion which completely offsets the $400,000 capital gain from the sale of the home.

The situation may arise where a client owns and alternates between two separate residences. The Elder Law practitioner may frequently encounter such an arrangement when advising the "snowbird" client (i.e., dividing the year between New York and Florida). In such a case, IRC § 121 will apply to the sale of the residence that the client uses the majority of the year.[58] In addition to the client's use of the property, other relevant factors in determining a taxpayer's principal residence include (1) the taxpayer's place of employment; (2) the principal place of abode of the taxpayer's family members; (3) the address listed on the taxpayer's federal and state tax returns, driver's license, automobile registration, and voter registration card; (4) the taxpayer's mailing address for bills and correspondence; (5) the location of the taxpayer's banks;

and (6) the location of religious organizations and recreational clubs with which the taxpayer is affiliated.[59]

> ***Example 3*****:** Ned owns 2 residences, one in New York and one in Florida. From 1999 through 2004, Ned lives in the New York residence for 7 months and the Florida residence for 5 months of each year. In the absence of facts and circumstances indicating otherwise, the New York residence is Ned's principal residence and he would be eligible for the § 121 exclusion of gain from the sale of the New York residence, but not the Florida residence.[60]

Most importantly, however, is the special treatment afforded by IRC § 121 for a client residing in a nursing home.[61] Specifically, if a client (1) becomes physically or mentally incapable of self-care, and (2) owns and uses a principal residence during the preceding five year period for periods aggregating at least 1 year, *then* the client is treated as using such property as a principal residence during any time in which the taxpayer owns the property and resides in any facility (including a nursing home) licensed by a State or political subdivision to care for such an individual.[62]

For those taxpayers that fail the aggregate 2 out of 5 year ownership and use test or the 2 year prior sale limitation, IRC § 121 provides a hardship exception with a reduced capital gains exclusion *if* the sale is a result of a change in place of employment, health or due to any other unforeseen circumstance.[63] The reduced capital gains exclusion is computed by multiplying the applicable capital gains exclusion amount (i.e., $250,000 or $500,000) by the following fraction: the shorter of the aggregate periods (during the 5-year period ending on the date of such sale) such property has been owned and used by the taxpayer as the taxpayer's principal residence, *or* the period of time between the date of the most recent prior sale for which IRC § 121 applied and the date of the instant sale, divided by 2 years.[64]

> ***Example 4*****:** Ned's father has a chronic disease. In 2003 Ned and Sally purchase a house that they use as their principal residence. In 2004 Ned and Sally sell their

> house in order to move into the house of Ned's father so that they can provide the care he requires as a result of his disease. Because, under the facts and circumstances, the primary reason for the sale of their house is the health of Ned's father, Ned and Sally are entitled to claim a reduced maximum exclusion under section 121(c)(2).[65]

Finally, if the principal residence, or the remainder therein, is owned by a trust that qualifies for "grantor trust status" pursuant to IRC § 671 through § 679, then the grantor is treated as the owner the residence for purposes of IRC § 121. This will insure that the grantor is entitled to the capital gains exclusion if the IRC § 121 conditions are met.[66]

1. Tax Basis Issues – Stepped up basis until January 1, 2010.

It is vital for the Elder Law practitioner to recommend a vehicle to transfer the family home that will provide the beneficiary with a step up in tax basis at the grantor's death. Basis is the benchmark for determining gain or loss on the sale or exchange of an asset. A bare transfer of the family home either outright or in trust to the beneficiary, without a retained interest or power, will cause the beneficiary to generally inherit the grantor's cost basis plus capital improvements.[67] In the event that the beneficiary does not qualify for the IRC § 121 capital gains exclusion when the property is sold, there can be a tremendous capital gains problem for the beneficiary.

> ***Example 5:*** Ned has a chronic condition that requires his placement in a nursing home within the next two years. Ned owns a home White Plains which he purchased in 1958 for $20,000 in which he has made $20,000 in improvements. Ned transfers the home outright to his daughter, Joanne, who lives in Albany. Joanne sells the house five years later for $500,000 and she still lives in Albany. Since Joanne does not qualify for the IRC § 121 exclusion on Ned's home, she must pay a capital gains tax on the $460,000 gain.

Instead, if the Elder Law practitioner simply reserves a life estate for the grantor on the deed of transfer, the beneficiary will enjoy a step up in basis to the fair market value of the property at the grantor's death.[68] In particular, IRC § 1014(a) permits the step up in basis for

property acquired by a beneficiary from a decedent's estate.[69] IRC § 2036 expressly provides that the decedent's gross estate shall include the value of all property, to the extent of any interest therein, that the decedent transferred by trust or otherwise, and retained a life estate. Thus, the transfer by deed reserving a life estate may eliminate the capital gains tax problem in Example 5, above.

> ***PRACTICE POINTER*****:** If the family plan is to sell the home prior to the death of the A/R (and retention of property tax exemptions is not a concern), then transferring the home subject to a life estate may serve no purpose other than to expose the A/R's life estate value to Medicaid recovery. Instead, if the Elder Law practitioner transferred the property into a qualifying trust, then the liquidated life estate value may be protected from recovery since it is paid to the trustee.

Alternatively, the Elder Law practitioner may recommend transferring the home through a deed (or to a trust) that retains a special power of appointment. A special power of appointment is a power in which the grantor reserves the right to alter, amend or terminate beneficial interest in the property to a class of beneficiaries other than the grantor, her estate, or the creditors of her estate. The reservation of such a special power of appointment will subject the home to inclusion in the grantor's gross taxable estate which, in turn, will give the beneficiaries of the home a step up in basis.[70]

It is important to note, however, that on January 1, 2010, IRC § 1014 will be replaced with carryover basis under IRC § 1022. The Elder Law practitioner is urged to advise clients that the elimination of a stepped up basis in 2010 will return the capital gains problem for the beneficiary to full view even with a reserved life estate and/or special power of appointment.

B. Estate Tax[71]

While the rhetoric that followed the debates and the enactment of Economic Growth and Tax Relief Reconciliation Act of 2001 ("EGTRRA") focused on the supposed repeal of the estate and

GST taxes, these taxes appear to remain alive and well. In fact, EGTRRA merely provides a temporary reprieve from the burdens (unjust or not) of the federal estate and GST tax system that comes in three forms. First, the applicable exclusion amount, which had been $675,000 in 2001 and slated to increase gradually to $1 million in 2006, was accelerated to that amount in 2002 and placed on a new time line, increasing to $3.5 million in 2009.[72] Second, pursuant to § 2010(c) of the Internal Revenue Code, the applicable exclusion amount and the GST exemption was unified on January 1, 2004,[73] and will remain as such until the year 2011. Finally, EGTRRA provides for repeal of the estate and GST taxes[74] *only* for the year 2010.

It is clear that the federal estate and GST taxes are not dead. Instead, despite an easing of the tax burden over the next seven years due to the rising exemption amounts and the one year repeal, the federal estate and GST taxes will re-emerge in 2011 in full force and effect under the pre-EGTRRA laws.

1. The price we pay for EGTRRA.

The temporary relief under EGTRRA does not come without a hefty price: the demise of the state death tax credit and the replacement of stepped-up basis with carryover basis.

a. Phase-out of the state death tax credit.

Prior to 2001, many states imposed a state estate tax that was equal to the state death tax credit allowed on the federal estate tax return.[75] Such states were often referred to as "pickup tax" states, since they would receive estate tax revenue to the extent that the federal government shared such revenue by means of a credit. As a result of EGTRRA, however, the state death tax credit was phased out through 2005. In particular, EGTRRA reduced the state death tax credit by 25% in 2002, by 50% in 2003, and by 75% in 2004, and repealed the state death tax credit for estates of decedents dying after December 31, 2004, replacing it with a deduction for state death

taxes paid.[76] Many "pickup tax" states, however, have enacted legislation "decoupling" their estate taxes from the federal tax changes, thereby allowing them to retain estate tax revenue. New York, for example, applies a state exemption amount of $1 million, and calculates the estate tax on estates over this amount using Table B -- Computation of Maximum Credit for State Death Tax, based on rates in effect in 2001,[77] despite the fact that that credit is being phased out. As a result, a taxable estate in New York and other such "pickup tax" jurisdictions that have decoupled will pay more in combined federal and state estate taxes due to the reduction in the state death tax credit.

> ***Example 6***: The Estate of an unmarried New York decedent who died in 2001 with a taxable estate of $2.5 million would have paid federal estate tax of $664,450 (after taking into account the applicable federal estate tax exemption of $675,000 available in 2001 and a credit of $138,800 for death taxes paid to New York State).
>
> ***Example 7***: Given the same facts as in Example 1, except that death occurs in 2004, the Estate would owe federal estate tax of $435,300 (after taking into account the federal estate tax exemption of $1.5 million then available and a state death tax credit of $34,700 (state death tax credit of $138,800 reduced by 75%). The Estate would also owe New York State estate tax in the amount of $138,800, despite the fact that the allowable credit for federal estate tax purposes would only be $34,700. [78]

2. The loss of a step-up in basis in favor of carryover basis.

For the year 2010, the one year the estate and GST taxes are repealed, EGTRRA terminates the step-up in basis for property acquired from a decedent and replaces it with a carryover basis.[79] Carryover basis is defined as the lesser of (i) the decedent's adjusted basis or (ii) the fair market value of the property at the decedent's date of death.[80] The decedent's executor can allocate a $1.3 million basis increase to any one or more assets for which carryover basis applies.[81] In addition to the $1.3 million basis increase, a spousal property basis increase of $3

million can be allocated to property transferred outright or in a qualified terminable interest property trust (“QTIP”).[82] Note, however, that the basis increase for any asset cannot exceed the fair market value of the asset at the decedent’s date of death.

While at first blush this may not appear significant, consideration must be given to the potential income tax consequence to the beneficiaries of the decedent’s estate when (i) the net appreciation of the decedent’s assets is greater than $1.3 million and there is no surviving spouse and (ii) the net appreciation is more than $4.3 million and there is a surviving spouse.

> ***Example 8:*** A widower dies in 2010 with the following assets in his name alone:
>
> | | Adjusted Basis | Fair Market Value |
> |---|---|---|
> | House | $200,000 | $1,500,000 |
> | Stock | 100,000 | 500,000 |
>
> His Will leaves his entire estate to his only child. If the decedent’s executor allocates the $1.3 million basis increase entirely to the house ($1.3 million + $200,000 = $1.5 million), and if the child later sells the stock, the child will incur a long term capital gain of $400,000 and a capital gains tax of $80,000. ($500,000 - $100,000 = $400,000; $400,000 x 20% = $80,000).[83] Note that the one year repeal of estate and GST taxes under EGTRRA comes with an attached income tax liability. In addition, New York State will impose a state estate tax in the amount of $99,600.
>
> ***Example 9***: Compare the results in Example 3 to those that would occur if the same decedent were to die in 2006 when the federal applicable exclusion amount increases to $2 million. There would be no federal estate tax although New York would still collect its pickup estate tax of $99,600 and, since the child would receive an aggregate step-up in basis to $2 million in the house and the stock to their fair market value on date of death (or alternate valuation date), there would be no income tax liability.

Another drawback to the carryover basis system is the potential for fiduciary issues to arise when administering the estate of a decedent who dies in 2010. In particular, unless detailed and complete records regarding basis are maintained during the decedent’s lifetime, the decedent’s

executor will have the overwhelming task of attempting to reconstruct the basis in order to satisfy the reporting requirements. Not only will this effort involve additional time and fees, but it will also expose the executor to an enhanced risk of being surcharged.[84] The executor may also be subject to claims by beneficiaries in different tax brackets that the allocation of the basis increase is neither fair nor reasonable.[85]

Many of these issues were previously addressed following the Tax Reform Act of 1976 when carryover basis was initially introduced. Plagued with problems then, it could not pass muster and, within a few years, was repealed retroactively. Given that the 1976 carryover provisions failed despite the fact that they provided a "fresh start" date for determining basis (rather than requiring one to make that determination from old and/or incomplete records), as well as the fact that carryover basis under EGTRRA is staged for only a one year come back, it is particularly difficult to expect clients to pay legal fees for provisions that may never take effect. Nonetheless, as we get closer to the year 2010, we must assess with our clients – particularly those who are frail or who may not remain competent over the next few years – the appropriateness of the retained life estate and special power of appointment as a means to obtain a step up in basis.

C. Gift Tax

Due to the increase in the federal gift tax applicable exclusion amount to $1 Million per person ($2 Million for a married couple), gift taxes may be of little concern in the context of Medicaid planning for the home. Obviously, the exception to this would be downstate where the value of even modest homes are approaching $1 Million. In such a case, the value of any gifted

home that exceeds $1 Million would require the filing of a federal gift tax return and the payment of a gift tax.

A transfer of the home to a family member[86] utilizing a life estate deed will carry a different gift tax value than a transfer to a non-family member. In particular, the retained life interest[87] in the home transferred to a family member will have a value of zero; thus, the fair market value of the home is the value of the gift.[88] Whereas, the value of the gift when the remainder interest is transferred to anyone other than a family member will be discounted based upon the fair market value of the property, less the actuarial value of the retained life estate pursuant to IRC § 7520 and regulations promulgated thereunder.[89] Nothwithstanding the differing valuation methods, a transfer of the home by a life estate deed is a completed gift upon transfer.

In the context of Medicaid planning, however, the transfer of the home reserving a life estate is only a partially uncompensated transfer (i.e., A/R receives a discount).[90] The value of the uncompensated transfer, which is utilized to determine the Penalty Period resulting from such a transfer, is based upon an actuarial calculation using the HFCA life estate and remainder interest table.[91]

> ***Example 10*****:** Ned, a 73 year old man, resides in Westchester County and transfers his home that has a fair market value of $450,000 to his son, Tom. By virtue of this transfer, Ned created a Penalty Period of 54.01 months ($450,000/$8,332 = 54.01).
>
> ***Example 11*****:** Same facts as Exhibit 10, however, instead of an outright transfer to Tom, Ned reserves a life estate. This transfer only causes a Penalty Period of 24 months (Remainder interest factor for a 73 year old is .44429. $450,000 x .44429 = $199,930.50 – remainder interest value. $199,930.50/$8,332 = 24 months.

In certain circumstances, the Elder Law practitioner may desire to avoid triggering a federal gift tax when transferring the home. This objective may be achieved by transferring the

property subject to a special power of appointment ("SPOA") in the grantor to appoint the principal to a class of beneficiaries other than the Settlor, her estate, or the creditors of her estate. [92] Importantly, from a Medicaid planning perspective, the reservation of a SPOA, either in the deed or trust, will not cause the property to be an available resource to the A/R.[93] This result will be frustrated, however, if the Elder Law practitioner mistakenly drafts a general power of appointment which among other negative tax consequences, may cause the home to be an available resource to the A/R and subject to Medicaid recovery.

Such a strategy may be important to the A/R where there are concerns that the A/R's descendants have potential creditor (i.e., financial or marital), substance abuse, and/or chronic illness issues. It is important to remember that when a life estate deed is conveyed, the grantor is giving a *fee interest* in the remainder. In contrast, however, the SPOA affords the grantor flexibility to remove or replace a remainderperson if facts are revealed that require the grantor to remove the beneficiary's name from the deed to preserve the home from the beneficiary's creditors. This may give the A/R a sense of control of their sacred asset by holding the beneficiary accountable to the A/R.

In the event that the grantor may require Medicaid in the near term, it may be beneficial, and a powerful planning strategy, to reserve a life estate on the deed and transfer the remainder, either outright or in trust, subject to a SPOA. By utilizing such an approach, the grantor not only receives the benefits of control, discussed above, but the grantor will benefit from a discounted gift value (i.e., a partially uncompensated transfer), explained above, in the remainder interest for Medicaid eligibility.[94]

1. Title Concerns.

Since a life tenant has the exclusive right to use and occupancy of the home, in the event the home is placed on the market, a title company will not find clear and marketable title unless the remainderperson can (a) demonstrate that the life tenant died by producing a death certificate and/or or affidavit; or (b) produce the life tenant at closing (or by fiduciary representative) to sign the deed conveying the life estate interest to the purchaser.

With regard to drafting the SPOA, however, the Elder Law practitioner must exercise extreme care not to cloud marketability or insurability of title. Since a special power of appointment may be exercised through an intervivos or testamentary declaration, it is imperative that the drafting attorney eliminate the minefield of title issues that may result from the exercise of a testamentary SPOA. This may be accomplished by limiting the exercise of the SPOA to an intervivos deed transfer.[95] Further, the drafting attorney should limited the class of permissible appointees to a narrowly defined class of competent adult beneficiaries.[96] A combination of these suggestions may alleviate a cloud on title caused by a potential incapacitated appointee (i.e., chronically incapacitated or minor appointee). Thus at closing, the new deed may be executed by the life tenant, the remainderpersons, and all permissible appointees.[97]

> ***DRAFTING TIP*:** *The following is language to consider when drafting the SPOA permitting only an intervivos exercise:*
> "The Grantor reserves the power to appoint, in whole or in part, the Property to or for the benefit of any one or more of the Grantor's adult issue with legal mental capacity, in such proportions, outright or on such trusts, terms, and conditions as the Grantor may specify. The Grantor must exercise this special power of appointment by a writing executed and acknowledged during his/her lifetime and recorded in the [Clerk's Office] within one hundred twenty (120) days of the date of such exercise. This special power of appointment may not be exercised by the Grantor's Last Will and Testament or Codicil. A release of the power reserved hereunder, in whole or in part, shall be effective when recorded with the [Clerk's Office]. Any exercise or release of the foregoing powers may be made by the Grantor's agent acting under a durable power of attorney."

> ***DRAFTING TIP**: The following is language to consider when drafting the SPOA permitting a testamentary or an intervivos exercise:*
> "The Grantor reserves the power to appoint, in whole or in part, the Property to or for the benefit of any one or more of the Grantor's adult issue with legal mental capacity, in such proportions, outright or on such trusts, terms, and conditions as the Grantor may specify. The Grantor must exercise this special power of appointment by a writing executed and acknowledged during his/her lifetime and recorded in the [Clerk's Office] within one hundred twenty (120) days of the date of such exercise, or by his/her last Will or Codicil making specific reference hereto. If this special power of appointment is exercised by the Grantor's Last Will and Testament or Codicil, the failure to record notice of any such exercise of this power in the [Clerk's office] within one hundred twenty (120) days of the Grantor's death shall be conclusively treated as a default in the exercise of the power. A release of the power reserved hereunder, in whole or in part, shall be effective when recorded with the [Clerk's Office]. Any exercise or release of the foregoing powers may be made by the Grantor's agent acting under a durable power of attorney."

D. Property Tax Exemptions

An opportunity exists for the Elder Law practitioner to preserve, through careful drafting, any senior citizen enhanced STAR exemption, the regular STAR exemption, veterans exemption or other tax credits that the A/R may enjoy on the family home property. The Elder Law practitioner should avoid unnecessary verbosity on the deed and, instead, heed sound advice – keep it simple! The soundness of this advice can be gleaned from the New York State Office of Real Property Services Opinions of Counsel ("SBRPS"), which provide guidance to tax assessors regarding the interpretation of deed language.

In particular, if a "person holds a life estate in real property, he or she must be considered the legal owner of the property, both for purposes of the designation of the owner on the assessment roll…and for purposes of exemption administration…"[98] Simply, the key to drafting the life estate is to explicitly mention it on the deed.[99] Alternatively, albeit less clear, the drafter may provide for a grant of "use and possession" of the property for the A/R's life. The fundamental nature of a life estate is that it conveys to the grantee not only the right to occupy,

but also the right to receive the rents and profits of the property and to pay charges such as taxes, repairs, and insurance.[100]

In contrast, however, a right of occupancy grants nothing more than the right to occupy the premises.[101] Poor drafting which has been interpreted as merely a right of occupancy (and not entitling grantee to tax exemptions) include the right to "make their home on the premises," "occupy the premises," and the "right to live in the premises."[102] The threshold for determining whether a deed reserves a life estate or merely a right of occupancy hinges upon the parties' intent in the document.[103]

Equally important, the SBRPS expressed an opinion regarding a Medicaid planning case in the face of 96 ADM-8.[104] In that opinion, the SBRPS stated while a life estate may have value when a life interest is sold pursuant to 96 ADM-8, a life interest cannot be created for assessment roll purposes if a fee simple deed is conveyed and a separate document from the fee holder to the grantor attempts to create a life lease if such document does not qualify as a conveyance under real property law (i.e., naming a specific grantor and grantee, a proper designation of the property, and recital of consideration).[105]

Further, a deed which purports to prohibit the grantee's ability to assign the life estate or sublease the same will not be viewed as a life estate for tax assessor roll purposes.[106] Similarly, a deed that reserves a non-exclusive right to use the property for life is not a life estate interest since the life tenant must have exclusive use of the property.[107]

> ***DRAFTING TIP*:** *For simplicity and clarity, consider the following language for a life estate deed:* "A life estate is hereby reserved by and for the life of [NAME], the party of the first part herein."

> ***DRAFTING TIP*:** *Alternatively, if compelled to describe the rights of the life tenant, consider:* "The Grantor, [NAME], reserves a life estate in the above said Property during his/her lifetime. During Grantor's lifetime, the Grantor shall

have the exclusive right to the use and occupancy of the Property, to lease, let, or license the same, and to all rents, income, fees, or profits generated from the said maintenance, fees, charges, and expenses relating to the premises and shall pay all taxes assessed or imposed with respect thereto, and all interest on any mortgages thereon.

PRACTICE POINTER: It may be difficult to convince certain counties in New York to recognize a life estate interest established in a trust (i.e., Nassau County); thus, it is recommended that the Elder Law practitioner consult with the county assessors office *prior* to effectuating any transfer of the family home. In those counties where a life estate interest in a trust will not be recognized for purposes of the tax assessment roll, consider utilizing a deed which explicitly reserves a life estate and conveys a remainder interest to the trust. While this may expose the life estate value to Medicaid recovery in the event of a sale, the property tax exemptions will be preserved. In those counties where a life estate interest will be recognized in the trust document because the exemption status will be determined on the basis of the trust beneficiary's status, be certain to draft a trust provision that explains the right of exclusive life use.[108] While Medicaid generally may not afford the same discount given to the remainder interest on a life estate deed for eligibility purposes, if the home is sold during the lifetime of the A/R, then the proceeds will not be exposed to Medicaid as they would in the life estate deed.

IV. Conclusion.

The Elder Law practitioner must guide the client through the maze of Medicaid lien, recovery and eligibility rules while not taking their eye off the income, estate, gift, and property tax ramifications when suggesting a plan of action to preserve the home. If adequately informed by the Elder Law practitioner, it is clear that the client has a range of options to consider when protecting the home, a successful combination of which will bring piece of mind and comfort to the client.

---

[1] The author would like to acknowledge the significant contributions and knowledge of Louis W. Pierro, Esq. and Steven A. Schurkman, Esq. in preparation of this article.

[2] Medicaid can always place a lien on property of an A/R pursuant to a judgment of a court on account of Medicaid incorrectly paid. 42 U.S.C.A. § 1396p(a)(1)(A) (West 2005); Social Services Law § 369(2)(a)(i)(McKinney's 2005).

[3] 42 U.S.C.A. § 1396p(a)(1)(B); Social Services Law § 369(2)(a)(ii). *See also* 02 OMM/ADM-3, pg. 7 (April 17, 2002).

[4] *E.g. Anna W. v. Bane*, 863 F.Supp. 125, 129-130 (W.D.N.Y. 1993).

[5] 42 U.S.C.A. § 1396p(a)(3); Social Services Law § 369(2)(a)(ii). *See also* 02 OMM/ADM-3 at 7.

[6] 42 U.S.C.A. § 1396p(a)(A); Social Services Law § 369(2)(a)(ii)(A).
[7] 42 U.S.C.A. § 1396p(a)(B); Social Services Law § 369(2)(a)(ii)(B).
[8] 42 U.S.C.A. § 1396p(a)(C); Social Services Law § 369(2)(a)(ii)(C).
[9] *See* Attachment I to 02 OMM/ADM-3.
[10]*Id.*
[11] *Id.*
[12] 18 NYCRR § 360-4.4(c)(2)(iii)(b); 02 OMM/ADM-3 at 7.
[13] 02 OMM/ADM-3 at 7.
[14] *Id.*
[15] *See* Attachment II to 02 OMM/ADM-3.
[16] *Id.*
[17] *See* Attachment III to 02 OMM/ADM-3.
[18] 96 ADM-8 at 21 (March 29, 1996).
[19] *Id.*.
[20] *In the Matter of D.C.*, Fair Hearing No., 3030224R (December 7, 1998).
[21] Social Services Law § 369(2)(b)(i)(A).
[22] Social Services Law § 369(2)(b)(i)(B). Medicaid may recover for services provided within the preceding ten (10) years of the A/R's death. Social Services Law § 104(1).
[23] Social Services Law § 369(2); Social Services Law § 366(3); Social Services Law § 104. *E.g. Matter of the Estate of Craig*, 82 N.Y.2d 388, 624 N.E.2d 1003, 604 N.Y.S.2d 908 (N.Y. 1993); *Commissioner of Dept. of Social Servs. of City of N.Y. v. Fishman*, 275 A.D.2d 599, 713 N.Y.S.2d 152 (1st Dept. 2000), *appeal after remand*, 280 A.D.2d 396, 720 N.Y.S.2d 493 (1st Dept. 2001); *Commissioner of the Dept. of Social Servs. of City of N.Y. v. Spellman*, 243 A.D.2d 45, 672 N.Y.S.2d 298 (1st Dept. 1998); *Matter of Imburgia*, 130 A.D.2d 658, 515 N.Y.S.2d 590 (2d Dept. 1987).
[24] Social Services Law § 104-b; Social Services Law § 369(2)(c).
[25] Social Services Law § 369(3).
[26] Social Services Law § 369(2); Social Services Law § 366(3); Social Services Law § 104. *E.g. Matter of the Estate of Craig*, 82 N.Y.2d 388, 624 N.E.2d 1003, 604 N.Y.S.2d 908 (N.Y. 1993); *Commissioner of Dept. of Social Servs. of City of N.Y. v. Fishman*, 275 A.D.2d 599, 713 N.Y.S.2d 152 (1st Dept. 2000), *appeal after remand*, 280 A.D.2d 396, 720 N.Y.S.2d 493 (1st Dept. 2001); *Commissioner of the Dept. of Social Servs. of City of N.Y. v. Spellman*, 243 A.D.2d 45, 672 N.Y.S.2d 298 (1st Dept. 1998); *Matter of Imburgia*, 130 A.D.2d 658, 515 N.Y.S.2d 590 (2d Dept. 1987). OMM GIS 04 MA-033.
[27] *Id.*
[28] *Id.*
[29] Social Services Law § 369(2)(b)(ii); 02 OMM/ADM-3 at 7.
[30] Social Services Law § 369(6).
[31] *Id.*
[32]Social Services Law § 369(2)(b)(ii); 02 OMM/ADM-3 at 7.
[33] *Id.*
[34] Social Services Law § 369(2)(b)(iii)(A); 02 OMM/ADM-3 at 7.
[35] Social Services Law § 369(2)(b)(iii)(B); 02 OMM/ADM-3 at 7.
[36] 18 NYCRR § 360-4.4(c)(2)(iii)(b); 02 OMM/ADM-3 at 7.
[37] Social Services Law § 369(5).
[38] 02 OMM/ADM-3 at 8. There are other instances were recovery or a waiver from recovery is available (i.e., native Americans), however, the author refers the reader to 02 OMM/ADM-3 for a resuscitation of the same.
[39] *Id.*
[40] Social Services Law § 367-f. 02 OMM/ADM-3.
[41] Social Services Law § 369(2)(i); 18 NYCRR § 348.4 and 352.31(d)(5).
[42] *Oxenhorn v. Fleet Trust Co.*, 94 N.Y.2d 110 (1999).
[43] 96 ADM-8 at 21.
[44] *Id.*
[45] *See Id.*, Attachment V.
[46] 96 ADM-8 at 21.

[47] *Id.*
[48] *Id.*
[49] Social Services Law § 366(5)(d)(4); 18 NYCRR 360-4.4(c)(2)(iv).
[50] OMM GIS 04 MA/033.
[51] Social Services Law § 366(5)(d)(3)(i)(A)-(D); 18 NYCRR 360-4.4(C)(2)(iii)(8)(1)-(4).
[52] Revenue Ruling 84-43.
[53] IRC § 121(a) (BNA 2005)(emphasis added).
[54] *Id.*
[55] IRC § 121(b)(1).
[56] IRC § 121(b)(2)(A).
[57] IRC § 121 (b)(3)(A).
[58] U.S. Treas. Reg. § 1.121-1(b)(2).
[59] *Id.*
[60] U.S. Treas. Reg. § 1.121-1(b)(4), Example 1.
[61] IRC § 121(d).
[62] *Id.*
[63] IRC § 121(c).
[64] IRC § 121(c)(1)(B)(i).
[65] U.S. Treas. Reg. § 1.121-3(d), Example 2.
[66] U.S. Treas. Reg. § 1.121-1(c)(3)(i).
[67] IRC § 1015.
[68] IRC § 1014(a).
[69] *Id.*
[70] IRC § 2038(a); IRC § 1014(b)(3).
[71] The following section was adapted from an article written by this author and Susan Taxin Baer titled "Flexibility and Simplicity: The Drafting Keys after EGTRRA 2001," New York State Bar Association Trusts and Estates Law Section Newsletter, Vol. 36, No. 3 at 18-22 (Fall 2003).
[72] I.R.C. § 2010(c). In addition, EGTRRA provides that the top marginal estate and gift tax rate will decrease from 55% in 2001 to 45% in 2009, but the top marginal estate and gift tax rate will return to 55% in 2011. In the year 2010, when the estate tax is repealed, the gift tax will be retained at the top income tax rate.
[73] § 2631(c). It is at this point in time that the estate tax and gift tax will be "de-unified" (although they will share a common tax rate from 2002-2009).
[74] It is important to note that this repeal does *not* include the federal gift tax. The federal gift tax applicable exclusion amount will remain at $1,000,000 with a maximum tax rate in 2010 of 35%.
[75] § 2011(a).
[76] §§ 2011(b)(2)(B), 2058.
[77]Technical Services Bulletin Memorandum, TSB-M-02(2)M (March 21,2002), which allows New York to take advantage of the federal estate tax exemption of $1 million for decedents dying in 2002 and 2003, despite the fact that §951 of the New York Tax Law might otherwise be interpreted as limiting the exemption to $700,000 for the years 2002 and 2003.; *see also* NYS Estate Tax Return, Form ET-706 (3/02).
[78] For an excellent discussion of the effect of EGTRRA on New York estate tax calculations, *see* NYSBA Trusts and Estates Law Section Newsletter: Philip L. Burke, *The Effect of Recent Federal Estate Tax Legislation on the New York Estate Tax: Part II*, Winter 2002, vol. 35, no. 4, at 40.
[79] § 1014(a), (f).
[80] § 1022(a)(2).
[81] § 1022(b)(2)(B). In addition, §1022(b)(2)(C) provides that the basis increase shall be further increased by unused built-in losses and capital loss carryovers.
[82] § 1022(c)(2)(B).
[83] This example does not take into account the recent decrease in the capital gains tax rates before the new carryover basis rules under EGTRRA take effect.
[84] Frank S. Berall, Ellen K. Harrison, Jonathan G. Blattmachr, and Lauren V. Detzel, *Planning for Carryover Basis that Can Be/Should Be/Must be Done Now*, WG&L Estate Planning Journal (March 2002).
[85] *Id.*

[86] IRC § 2701(e)(1)(member of family includes the transferor's spouse, a lineal descendant of the transferor or the transferor's spouse, and the spouse of any such descendent).
[87] IRC § 2702(c)(3)(A).
[88] IRC § 2702(a)(2)(A).
[89] IRC § (a)(2)(B).
[90] 96 ADM-8 at 20.
[91] 96 ADM-8, Attachment V.
[92] Treas. Reg. § 25.2511-2(b).
[93] *E.g. Verdow v. Sutkowy*, 209 F.R.D. 309 (NDNY 2002); *Spetz v. New York State Dept. of Health*, 190 Misc.2d 297, 737 N.Y.S.2d 524 (Chautauqua Cty 2002). *See also* GIS 04 MA/001 (1/20/2004).
[94] 96 ADM-8 at 20.
[95] *See* Louis W. Pierro, Esq., "Protecting the Home: Transfers of Real Property – Medicaid and Tax Considerations," Westchester County Bar Association, March 21, 2002.
[96] *Id.*
[97] For an exhaustive explanation of the title issues, *see*, "Deeds with Reserved Powers of Appointment: Do the Benefits Outweigh the Pitfalls?", by Lawrence B. Lipschitz, New York Counsel to Lawyers Title Insurance Corporation, 1996. A copy of this article may be obtained from your title company's legal department.
[98] Volume 9, Opinions of Counsel SBRPS No. 41.
[99] *Id.*
[100] *Id.*
[101] *Id.*
[102] *Id.*
[103] Volume 10, Opinions of Counsel SBRPS No. 20 (reserving life estate subject to termination for failing to occupy property for a continuous 120 day period). *Compare with* Volume 9, Opinions of Counsel SBRPS No. 49 (exclusive life use so long as grantee continues to permanently reside on the property is a valid restriction to a life estate).
[104] Volume 10, Opinions of Counsel SBRPS No. 55.
[105] *Id.*
[106] Volume 10, Opinions of Counsel SBRPS No. 58.
[107] Volume 10, Opinions of Counsel SBRPS No. 102.
[108] Volume 10, Opinions of Counsel SBRPS No. 27; Volume 11, Opinions of Counsel SBRPS No. 44 (trust provision that permits the trustee to sell the home if trust beneficiary vacates for 2-6 months does not render trust ineligible for exemptions).