

9-1-2020

A Safe Harbor in the Medicaid Adventure: Lady Bird and Transfer on Death Deeds

Gerry W. Beyer

Follow this and additional works at: <https://scholarlycommons.law.hofstra.edu/actecj>



Part of the [Estates and Trusts Commons](#), [Taxation-Federal Estate and Gift Commons](#), and the [Tax Law Commons](#)

Recommended Citation

Beyer, Gerry W. (2020) "A Safe Harbor in the Medicaid Adventure: Lady Bird and Transfer on Death Deeds," *ACTEC Law Journal*: Vol. 46: No. 1, Article 3.

Available at: <https://scholarlycommons.law.hofstra.edu/actecj/vol46/iss1/3>

This Article is brought to you for free and open access by Scholarly Commons at Hofstra Law. It has been accepted for inclusion in ACTEC Law Journal by an authorized editor of Scholarly Commons at Hofstra Law. For more information, please contact lawlas@hofstra.edu.

A Safe Harbor in the Medicaid Adventure: Lady Bird and Transfer on Death Deeds

*Gerry W. Beyer**

I. INTRODUCTION

For many elderly individuals, a carefully crafted estate plan is a legal journey which contains personal and real property that passes outside the probate process to gain eligibility for Medicaid and/or avoid Medicaid estate recovery. Often, the family home is the largest asset individuals over the age of 65 own and inter vivos trusts serve as the traditional non-probate transfer mechanism. However, this method may add complexity and cost for those with limited resources. Alternatively, an individual may use a traditional deed to retain a life estate and transfer the remainder interest. However, the drawback of these deeds is that they may not be revoked or changed after execution. Modern law now provides two alternatives: Lady Bird Deeds and Transfer on Death Deeds. This article explores the advantages and disadvantages of each and how elderly individuals may benefit from their use.

II. LADY BIRD DEEDS

A. What Are They?

“Lady Bird Deeds” (LBD), also called “enhanced life estate deeds,” “revocable life estate deeds,” or “deeds with a reservation of a life estate with a general power of appointment,” are deeds in which the grantor retains a life estate and transfers the remainder interest while retaining the ability to revoke or alter the deed without the consent of the remainder beneficiary.¹ The name “Lady Bird” is not connected to President Lyndon B. Johnson’s wife, Lady Bird Johnson. Instead, its inception arose in 1982 from the elder law materials of Florida attorney

* Governor Preston E. Smith Regents Professor of Law, Texas Tech University School of Law. B.A. 1976, Eastern Michigan University; J.D. 1979, Ohio State University; LL.M. 1983 & J.S.D. 1990, University of Illinois. The author acknowledges the excellent assistance of William Langford, 2021 J.D. Candidate, Texas Tech University School of Law.

¹ 51 MOLLY DEAR ABSHIRE ET AL., TEX. ELDER L., TEX. PRAC. SERIES, § 9:32 (2020).

Jerome Solkoff.² Solkoff used fictional characters when explaining the utility of LBDs with one of them being Lady Bird. LBDs are executed following the same formalities as traditional life estate deeds. The revocability of the deed and control of the property the grantor retains provide flexibility which separates the LBD from the life estate deed.

B. Benefits of LBDs

LBDs are primarily used to assist elderly individuals to avoid a Medicaid transfer penalty and Medicaid estate recovery. When a grantor attempts to qualify for Medicaid assistance, the grantor must disclose asset transfers for less than fair market value within the look-back period (typically five years).³ If the execution of a deed is considered a disqualifying transfer, it could limit or bar Medicaid assistance for a certain period. Because the grantor retains full control of the property, the homestead retains its exemption status (assuming state law provides an exemption) and the execution of a LBD is not deemed a transfer for Medicaid purposes.

After the grantor dies, Medicaid estate recovery is the process by which state governments attempt to recover payments to the Medicaid recipients. States must implement this process under the Omnibus Budget Reconciliation Act of 1993 (OBRA).⁴ However it allows the states to determine how to implement the process and how to define “estate.”⁵ Further, states decide whether to employ an expanded estate program that enforces recovery with Tax Equity Fiscal Responsibility Act (TEFRA) pre-death liens.⁶

Typically, a Medicaid beneficiary’s home is a probate asset and could be subject to Medicaid estate recovery. However, a transfer by way of a LBD is complete upon the grantor’s death and bypasses the probate process. Unless state law includes such non-probate property within its definition of “estate,” the LBD protects the home from the recovery process.

Elderly grantors without capacity have access to the benefits of non-probate deeds through their agents. Under the law of most states, an agent under a durable power of attorney has the authority to execute a LBD if determined to be part of a prudent estate plan. Additionally, the cost of using a LBD is modest compared to a will or trust.

² See Kary C. Frank, *Ladybird Deeds*, 95 MICH. B.J., June 2016, at 30, 30-31.

³ 42 U.S.C. § 1396p(c)(1)(A), (c)(1)(B)(i).

⁴ *Id.* § 1396p(b); see also Robert C. Anderson, *Comparing Key Strategies in Owning the Home: Estate Planning, Tax and Medicaid Considerations – Part Two*, 220 ELDER L. ADVISORY, June 2009, at 1, 5.

⁵ § 1396p(b)(4).

⁶ Anderson, *supra* note 4.

LBDs provide a layer of protection against a remainder beneficiary's creditors. The limited property interest of the beneficiary makes it difficult for creditors to make a claim against the property, and the grantor may revoke or modify the LBD at any time if such an event occurs.

Because a LBD is not a completed gift, the beneficiary's income tax basis in the property is stepped-up to the fair market value upon the grantor's death.⁷ A future sale of the property would only trigger capital gains taxes on the increase in value accruing after the grantor's death.

C. Potential Problems with LBDs

Many states have yet to address whether they will give effect to a deed in which the grantor retains the right to take back all of the remainder beneficiary's interest. Further, as common-law based deeds, LBDs lack a standard form which greatly increases the chance of improperly prepared documents without professional help.⁸ These difficulties arose recently when families impacted by hurricanes had to "unwind" LBDs to place ownership of the real property in one person to qualify for recovery assistance.⁹

Although only an unsecured creditor in the hierarchy of claims, some title companies take the position that the Medicaid Estate Recovery statute creates superior rights for the state. These companies may require the joinder of remainder beneficiaries, and/or a written release from the state to insure title.¹⁰

Finally, because a LBD transfers a remainder interest to the beneficiary immediately, a mortgage holder could view the LBD as triggering a due-on-sale/transfer clause.¹¹ A grantor is unlikely to have the funds to make the payment and could lose the property in foreclosure proceedings.

III. TRANSFER ON DEATH DEEDS

A. What Are They?

A "transfer on death deed" also called a "beneficiary deed" is a statutorily authorized deed that allows a grantor to name a beneficiary

⁷ See I.R.C. § 1014(a)(1).

⁸ See Danaya C. Wright & Stephanie Emrick, *Tearing Down The Wall: How Transfer-On-Death Real-Estate Deeds Challenge The Inter Vivos/Testamentary Divide*, 78 MD. L. REV. 511, 533-37 (2019) (illustrating that customizable deeds must be drafted carefully).

⁹ Lucy Wood, *Transfer on Death Deeds in Texas: High Time for the TODD*, 9 EST. PLAN. & COMMUNITY PROP. L.J. 59, 72 (2016).

¹⁰ *Id.* at 73.

¹¹ *Id.* at 77.

who will obtain title to the property upon the owner's death.¹² While similar to the LBD and sometimes referred to as a "statutory LBD," the two instruments differ in that the beneficiary of a TODD does not own an interest in the property while the grantor is alive. Twenty-eight states and the District of Columbia have some form of TODD statute, and fifteen of these states and the District of Columbia have adopted the Uniform Real Property Transfer on Death Act.¹³

As statutory creations, TODD execution varies depending on the state enabling statute. Typically, the deed must contain an express provision that the transfer is to occur upon the death of the grantor if the beneficiary outlives the grantor. Unless the state has an applicable anti-lapse statute, the deed is ineffective if the beneficiary predeceases the grantor.

A TODD does not vest legal or equitable title in the beneficiary until the death of the grantor; therefore, neither the beneficiary nor the beneficiary's creditors may reach the property until the grantor's death. The grantor retains full control of the property and upon the grantor's death, the beneficiary owns the property subject to all encumbrances and interests affecting the grantor's title.

The grantor may revoke a TODD at any time for any (or no) reason. In some states TODDs cannot be made irrevocable. Revocation can occur when the grantor revokes the deed outright, records a subsequent deed that expressly or impliedly revokes the existing TODD, or transfers the property within the grantor's lifetime. An alternative disposition of the property in a will is ineffective.

B. Benefits of TODDs

For elderly individuals, TODDs hold many of the same benefits and avoid some of the problems of LBDS. However, TODDs may also pose potential problems for individuals who use them.

A TODD is unlikely to impact the grantor's ability to qualify for Medicaid because it does not affect the grantor's interest while the grantor is alive. Further, the execution and recordation of a TODD is not considered a transfer for Medicaid purposes.¹⁴ Likewise, the property maintains any status it had as a homestead and exemption from Medicaid eligibility.

¹² Stephanie Emrick, Note, *Transfer on Death Deeds: It Is Time to Establish the Rules of the Game*, 70 FLA. L. REV. 469, 474 (2018).

¹³ Gerry W. Beyer, *Transfer on Death Deeds Survey*, AM. C. OF TR. & EST. COUNS. 1, 7, https://www.actec.org/assets/1/6/Transfer_on_Death_Deeds_Survey.pdf (last revised Sept. 21, 2020).

¹⁴ 42 U.S.C. §§ 1396p(c)(1), 1382b(a)(1).

A TODD functions similarly to a LBD by allowing the real property to avoid the probate process because the property is not part of the grantor's estate. Consequently, the property may avoid the Medicaid estate recovery process unless state law has special provisions pulling the property back into the grantor's estate. Because the property is not a completed gift until the donor dies, the beneficiary receives a stepped-up basis in the property just like a LBD.¹⁵

TODDs are primarily designed to assist elderly lay individuals because they are inexpensive to create. This is evidenced by the many state TODD statutes that provide a standardized form and provide an easy avenue for an individual to create the deed without the assistance of a legal professional.

Finally, unlike a LBD, a TODD does not make a current transfer of an interest. Thus, it is highly unlikely that a TODD will trigger a due/transfer-on-sale provision in a mortgage or deed of trust.

C. Potential Problems with TODDs

The statutory design that allows lay individuals to execute TODDs are fraught with the typical problems that may arise when a non-lawyer attempts to practice law. Elderly individuals may misunderstand the consequences of a TODD or benefit more from a different legal instrument. Also, if the grantor divorces from the grantee or has a change in feelings toward the grantee, the beneficiary designation remains in place until the grantor revokes the deed unless state law provides otherwise.

Additionally, the statutory structure of some states bar agents from creating a TODD. This could potentially affect elderly individuals who have created a durable power of attorney and lack the capacity to create a TODD themselves.

Guidelines are still being developed for how title insurance companies will deal with TODDs. Thus, a company may refuse to insure a title which is not subject to reasonable dispute. For example, it has been reported that some title companies require the beneficiary to execute a quitclaim deed for the grantor to obtain title insurance.¹⁶ Uncertainty also exists as to whether the TODD beneficiary is covered by the grantor's title policy, as a strict construction of the policy may forgo such coverage.¹⁷

¹⁵ I.R.C. § 1014(a)(1).

¹⁶ Pamela D. Orsak, *Save Me from Probate: Transfer on Death Deeds and Lady Bird Deeds*, in ST. B. OF TEX., 40TH ANN. ADVANCED EST. PLAN. & PROB. ch. 4, 1, 7 (2016).

¹⁷ *Id.* at 7-8.

IV. CONCLUSION

Typically, both the LBD and the TODD are used by elderly individuals who have only one major real property asset, their home. Those individuals with a low income or for whom traditional estate planning techniques would be uneconomic or a burden will likely find these deeds attractive. Additionally, Medicaid eligibility and Medicaid estate recovery avoidance make these two deeds especially attractive safe harbors for elderly individuals who want to prepare for long-term health care costs while allowing their family or other desired recipient to receive their home upon death. These are useful tools to assist elderly individuals with their estate plans but need to be carefully considered on a case-by-case basis.