Powers of Appointment

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Powers of Appointment

Introduction

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Introduction to POAs – 1 IV-B-(1)-1

- A power of appointment ("POA") is a right, granted under a legal instrument such as a will or trust, by a person referred to as the "donor," to a person referred to as the "donee" or "powerholder," which empowers that powerholder to designate who should receive interests in certain property, called the appointive property, subject to the POA.
- The person or persons who are eligible to receive the appointive property is called a "permissible appointee(s)."
- Although the powerholder can designate those who receive beneficial ownership interests in the appointive property, the powerholder does not own the property.
- If the powerholder does not exercise the power the appointive property may pass to a default person indicated in the POA called the "default taker."

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Introduction to POAs - 2

- Depending on the characteristics of the POA, it may result in the appointive property being included in the powerholder's gross estate, or not, and it might result in a gift tax consequence, or not.
- POAs can also have significant income tax planning implications.
- POAs are granted by a third party.
- POAs are a flexible and versatile tool that can be used to accomplish a variety of planning goals. Their common usage belies the incredible complexity and potential traps for the unwary when planning with POAs.

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Introduction to POAs – 3
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- There are two types of POAs defined by the scope of the power, a general power of appointment ("GPOA") and a limited power of appointment ("LPOA").
- This distinction is critical for the determination of both the tax consequences of the power, and creditor access to the property subject to the power. The distinction may, however, differ for purposes of state law creditor considerations and federal tax considerations, and each state's laws may differ as to how powers are treated for creditor purposes as compared to other state's laws.

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Introduction to POAs – 4
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- Determining which state law applies (e.g. the law of the donor's domicile or the law of the powerholder's domicile) can be critical, as state laws often differ. The same power, because of the limitation to an ascertainable standard, should not be treated as a GPOA for tax purposes.
- GPOAs at common law had no restrictions on permissible appointees.
- In contrast, tax law defines a GPOA specifically as a power that includes within the permissible appointees any one or more of the following: (1) the powerholder, (2) the powerholder's estate, (3) creditors of the powerholder, or (4) creditors of the powerholder's estate. Inclusion of any one of these four appointees should suffice to characterize any POA as a GPOA, unless an exception in the Code applies.

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Introduction to POAs – 5
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- A limited or special POA, referred to as a "LPOA," limits the class of potential appointees.
- Specifically, any power that does not permit the powerholder to appoint to any of the persons who would cause the power to be a GPOA, is a LPOA. Thus, if the powerholder cannot appoint to: (1) the powerholder, (2) the powerholder's estate, (3) the creditors of the powerholder, or (4) the creditors of powerholder's estate, then the POA is characterized as a LPOA.
- The broadest LPOA would be the power to appoint to anyone other than the above 4. In many instances, narrower LPOAs are crafted, e.g. giving the surviving spouse the right to appoint solely amongst the couple's descendants, or perhaps descendants and charities.

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Introduction to POAs - 6

- The broader the class of permissible appointees the more incentive the donor of the power may have to adding a safeguard to the exercise, e.g. the approval of a non-adverse party.
- In most instances there will be no taxation on the exercise of a LPOA. An exception might be the application of the Delaware tax trap

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Capacity, Elder Abuse and Undue Influence

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Capacity, Elder Abuse and Undue Influence 1 IV-B-(1)-6

- For the powerholder to validly exercise a POA, he or she must have sufficient legal capacity to do so.
- Note that this may have limited or even no bearing on a GPOA causing inclusion in the powerholder's estate, as discussed below. There may also be some considerations as to whether this reflects on whether the power is a mere naked power or sham transaction, as discussed below.
- While commentators have frequently pointed out the risks of creditors of a powerholder reaching a power under state law, the issues of undue influence and elder abuse on POAs, has not received sufficient attention.

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Capacity, Elder Abuse and Undue Influence

- When planning to integrate powers of attorney into trusts for 2020 flexibility and basis step-up practitioners should consider not only the risk of creditors of the powerholder or the powerholder misusing the power granted, but also the risk of elder financial abuse and/or undue influence of the powerholder.
- Family members or unscrupulous individuals will try to get the elderly or inform client to inappropriately grant (donor) a POA or to inappropriately exercise a POA (powerholder).
- Undue influence is often insidious and difficult to identify. This is another reason why it may be important to put safeguards in place.

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Capacity, Elder Abuse and Undue Influence

- Consider requiring that the elderly client can't exercise the POA unless he or she gets the consent of a non-adverse party, like a lawyer or family member who is not a beneficiary. That individual can provide some oversight and make sure that the elderly client isn't being taken advantage of.
- Because many clients may be tempted to make large transfers before the election infusing flexibility into irrevocable trusts to deal with uncertainty could be important. This may be achieved in large part by integrating various powers of appointment into irrevocable trusts. For example, settlors may grant limited powers of appointment so that the powerholder can effectively rewrite the trust. Be mindful of the risks that elder abuse and undue influence might pose.

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Powers of Appointment

Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
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- The mere existence of the GPOA will generally suffice to cause estate tax inclusion.
- The fact that the powerholder has no knowledge of the GPOA or is incapable of exercising the power at death (e.g. the powerholder is incapacitated), may not change the desired result of estate tax inclusion.
- "But there may not be the certainty that some think."
- "There are nuances and we should not assume that the law if fixed and clear, it may not be."
- If the donee of the power, the powerholder, is a complete stranger might a court find the GPOA to be a sham?

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-10

- In the Hurd case, the decedent was competent at the time the power was granted and remained competent for four years during which the power could have been exercised. The question as to whether the power granted by the trust was possessed by the decedent was not raised or addressed. Is it relevant that the powerholder was competent at the date of grant and for several following years to the possession of the power?

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-10

- The court in the Round case confirmed that incapacity does not extinguish a power of appointment, as incapacity may have been a temporary matter. Note that the incapacity of the decedent in Round began over 20 years after he was appointed co-trustee.
- In Round that the decedent did in fact possess the retained power that caused estate tax inclusion but did that power end before death as a result of incapacity? It is not clear from the rationale in Round that if a GPOA is granted to someone who is legally incapacitated at the time of the grant, and which incapacity is likely to be permanent, rather than temporary, whether the conclusion, based on a Round-type analysis, would differ. Generally courts have not wanted to decipher those nuances.

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-11

- The court in Fish noted that "*[t]he taxpayer agrees that the decedent possessed a general power of appointment…*" but was arguing that as the decedent had been incapacitated for 7 years prior to decedent's death.
- The Fish court was clear in that they "*…agree with the District Court that the competency of the decedent is immaterial in determining whether a lapse or release of the power occurred.*"
- As in the Hurd and the Round cases, the decedent was competent when she received the general power of appointment, and later became incompetent.
- The court did not analyze whether the decedent possessed the general power of appointment at grant, as that question was not raised by either party.

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-11

- The court in Bagley rejected the arguments made by the taxpayer, indicating "*Unless otherwise provided by the will, the existence of an interest in property is not conditioned on the exercisability of the interest by the decedent at the time of her death. Thus, it is of no relevance to the existence of an interest in property held as a trustee that the trust was not established. This conclusion is compelled by the many cases that have determined that the existence of a power to appoint is not dependent on the capacity of the decedent to exercise the power.*"

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-13

- Noel v. U.S., 380 U.S. 678 (1965), involved the question of whether a decedent possessed at his death any of the incidents of ownership in a flight insurance policy that he purchased and handed to his wife before boarding the airplane in which he died. The Court, in holding the insurance proceeds includible in the decedent's gross estate under section 2042 of the Code, made the following statement at page 684: '**It would stretch the imagination to think that Congress intended to measure estate tax liability by an individual's fluctuating, day-by-day, hour-by-hour capacity to dispose of property which he owns**.'

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
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- The Finley decision was vacated on procedural grounds but its legal reasoning was not challenged when it was overturned. Some practitioners have labeled Finley an "**outlier**," but it is discussed below as the court's analysis is something a cautious practitioner may wish to consider in planning for a GPOA.
- In Finley, Mildred B. Whitlock died testate on December 18, 1971, two months after her husband Lester J. Whitlock passed away on October 18, 1971. Lester's will established a trust for the benefit of Mildred, in which Mildred was provided a GPOA.
- At all times following Lester's death and until Mildred's subsequent death, Mildred was mentally disabled, and the parties agreed that she lacked the testamentary capacity to execute a will, or codicil or to exercise the testamentary GPOA.

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-15

- Finlay….If the decedent, personally or through a guardian, lacked legal capacity to act as trustee, taxation would have been improper."
- Unlike the decedents in Hurd, Noel and Bagley, Margaret Whitlock from the time of devise of the general power of appointment until her death lacked the legal capacity to exercise the general testamentary power of appointment. This prevented her from possessing a general power of appointment within the meaning of Section 26 U.S.C. § 2041(a)(2).

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-16

- Freeman
- "During his lifetime, subsequent to the establishment of the trust, decedent received periodic payments of income from the trust. Decedent never saw the trust instrument and was never informed about and had no actual knowledge of his rights under paragraph VII of the trust… Petitioner contends…that since decedent was not informed of and had no actual knowledge of the power granted to him under paragraph VII of the trust, the value of the trust should not be included in decedent's gross estate under section 2041(a)(2)… However, there was no indication in the stipulation that decedent was ever subject to any mental or physical disability that rendered him incapable of exercising his power…

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-16

- Freeman
- …This is not a case in which the decedent was unaware of the existence of the trust since he was receiving income distributions therefrom...Furthermore, the decedent unquestionably had the right to know of the existence of the power contained in paragraph VII of the trust and could have acquired that knowledge by simply requesting the same from the trustee... The existence of the power of appointment brings it within the ambit of section 2041(a)(2) [highlight added]."
- Might the above excerpts from the court suggest that if the decedent was intentionally prevented from learning of the POA that perhaps a different result might follow?

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-17

- Pennsylvania Bank Trust
- Decedent's husband passed away on February 9, 1965. The husband's will, which was signed in 1954 and amended via codicil in 1964 to remove decedent as a co-executor, provided for a trust to be established for decedent, which was designed to receive a marital deduction under the IRC Sec. 2056(b)(5) rules, which requires that the surviving spouse receive a GPOA.
- Are marital power of appointment trust cases to be treated differently because the quid pro quo of getting a marital deduction in the first estate is inclusion in the surviving spouse's estate via a GPOA?

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-22 – STEPS TO CONSIDER

- Practitioners may consider these steps:
- Corroborate that the powerholder has legal capacity on the grant of the GPOA, although this appears to be unnecessary based on several of the preceding authorities. Nonetheless, several of the authorities discussed above discussed fact patterns where the decedent had capacity when the power was granted. If the authorities that discussed the GPOA marital trust are considered as a distinguishable, then several of the authorities that found legal capacity irrelevant, would not be considered in the analysis of this issue. If the powerholder does not have capacity, perhaps the GPOA could expressly state that an agent under a power of attorney or guardian for the powerholder could exercise the GPOA on behalf of the powerholder, if the donor were comfortable with that.

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-22 – STEPS TO CONSIDER

- Consider giving notice of the existence of the GPOA to the powerholder. This might be accomplished by verbal communication, although transmission in a manner that the receipt can be acknowledged might be preferable. This could include sending a copy of the trust agreement via certified mail return receipt to evidence receipt. Perhaps an e-signature on a document acknowledging receipt might suffice. Perhaps emailing the instrument creating the GPOA with a read receipt may be adequate.
- Consider the possibility of making the powerholder a beneficiary of the trust and perhaps of even making distributions to the powerholder. That, as in the Freeman case above, might demonstrate knowledge of the trust's existence.

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Is Notice, Knowledge or Capacity of the Powerholder Necessary for Estate Inclusion?
1 IV-B-(1)-22 – STEPS TO CONSIDER

- Consider explaining to the client that there are uncertainties in the law as to the assured inclusion of a GPOA in the powerholder's estate to cause estate inclusion, that most or all authorities on the issue occurred when the tax laws were quite different then the current free-basing environment, and that the IRS or a court might argue the position in Finlay above.

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Secs. 6161 and 6166 and GPOAs

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Secs. 6161 and 6166 Estate Tax Deferral and GPOAs 1 IV-B-(1)-25

- If assets are included in the powerholder's estate can the powerholder's estate avail itself of Code Sec. 6161 or Code Section 6166 estate tax deferral? What of Code Section 2032A special use valuation? What of alternate valuation date values? It would seem these options should be available subject to the powerholder's estate meeting the requirements of that Code Section.
- Code Sec. 6166(b)(2) provides: "*For purposes of paragraph (1)—(A)Time for testing Determinations shall be made **as of the time immediately before the decedent's death***."

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Secs. 6161 and 6166 Estate Tax Deferral and GPOAs 1 IV-B-(1)-25

- Code Sec. 2041(a)(2) provides: "*To the extent of any property with respect to which the decedent has **at the time of his death** a general power of appointment created after October 21, 1942, or with respect to which the decedent has at any time exercised or released such a power of appointment by a disposition which is of such nature that if it were a transfer of property owned by the decedent, such property would be includible in the decedent's gross estate under sections 2035 to 2038, inclusive. For purposes of this paragraph (2), the power of appointment shall be considered to exist on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even though the exercise of the power takes effect only on the expiration of a stated period after its exercise, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised.*"

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Secs. 6161 and 6166 Estate Tax Deferral and GPOAs 1 IV-B-(1)-25

- Does the time for testing immediately before death of a qualifying business interest under 6166 disconnect from the 2041 saying inclusion is at time of death?
- If the 6166 testing is immediately before death is that before 2041 inclusion from a GPOA is effective?

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Termination of "Small" Trust

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Termination of a "Small" Trust
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- It is not uncommon for a trust to include a provision permitting the trustee to terminate the trust if it becomes too small to justify its continued administration. This may be characterized as a general power of appointment if the trustee is a current beneficiary.
- With the potential wave of 2020 planning consider including a provision to terminate a trust that is small, perhaps even the quantum of what constitutes "small" might be rethought to provide more flexibility.

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Prudent Investor Act and POAs

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Prudent Investor Act and POAs
1 IV-B-(1)-31

- The status of a trust as a grantor trust (or not), and to whom (e.g. settlor or beneficiary), is important for a trustee to evaluate in determining the steps necessary to comply with the Prudent Investor Act. This should be documented in an investment policy statement (IPS).
- Thus, it is recommended that practitioners identify the tax status of trust assets they are investing, and track changes in that status.
- Documenting the income and estate tax status of a trust, perhaps acknowledging the potential impact of POAs in the instrument, both before and after the exercise of a POA, may be useful to demonstrate that these implications are being considered in the investment plan. This may be protective of the trustee.

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Prenuptial Agreements and POAs

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Prenuptial Agreements and POAs
1 IV-B-(1)-28

- In some states, a spouse asserting an elective share claim may also reach property over which the other spouse held a GPOA even if it has not been exercised.
- Consider addressing possible POAs in prenuptial agreements and waiving the right.

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POAs Key to Accomplishing 2020 Planning Goals

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POAs Key to Accomplishing 2020 Planning Goals

- 2020 focus of estate planning is to create irrevocable trusts before the 2020 elections to use the current high temporary exemptions. A Democratic victory in 2020 may bring enactment of harsh estate tax legislation along the lines of the tax bill that Bernie Sanders proposed in early 2019 in which Congressman Gomez proposed later last year.
- Key to this planning will be creative and efficacious use of a range of different types of powers of appointment, both special (limited) powers of appointment, and general powers of appointment.
- Following discussion will use as a framework 7 common goals many clients may have for 2020 planning and identify how creative uses and applications of various powers of appointment may accomplish each of those goals.

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2020 Goal 1: Use of High Temporary Gift and GST Exemption Prior to the 2020 Election

- Don't include LPOAs that Could Taint Gift as Incomplete.
  - The irrevocable trusts that are crafted should not provide the settlor with LPOAs that could taint the transfers to the trust as incomplete gifts. IV-B-Pt 1-45
  - This use of limited powers has often been intentional in planning. For example, in a traditional Incomplete Non-Grantor ("ING") trust the settlor often retained a limited power so that the transfers to the trust would be incomplete for gift tax purposes. This was done where the settlor had used all his or her exemption or wished to preserve exemption for other plans. In this context the goal was often state income tax minimization, not removing assets from the settlor's estate. Instead use a non-grantor SLAT (a SLANT or SALTy-SLAT).

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2020 Goal 2: Preservation of Access to Assets Transferred to Irrevocable Trusts in 2020

- Many clients wish to use exemption but to preserve access to the assets transferred. Creative uses of powers of appointment can facilitate accomplish this key goal of access to assets transferred to irrevocable trusts to use exemption, will be necessary.
  - Loan power - If the trust is to be structured as a grantor trust the settlor could provide in the trust instrument a LPOA held in a nonfiduciary capacity to loan trust assets to the settlor with adequate interest but without adequate security. This is merely a special or LPOA. IV-B-Pt 1-42 and 44.
  - Tax Reimbursement - incorporate a tax reimbursement provision so long as permitted under applicable state law without allowing the creditors of the settlor access to the trust assets. This may be a discretionary distribution decision made by the trustee. This is a special POA held by the trustee in a fiduciary capacity.

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2020 Goal 2: Preservation of Access to Assets Transferred to Irrevocable Trusts in 2020

- SLAT - Create spousal lifetime access trust, or "SLAT," is a common tool for using exemption and maintaining access. Each spouse creates a nonreciprocal trust for the other spouse. See reciprocal trust doctrine below. Variations of SLATs will use various POAs to maintain access.
- DAPT - For clients of wealth levels were more access is desired than a SLAT can provide (and certainly for single clients without a spouse that could provide indirect access through a SLAT) some form of domestic asset protection trust ("DAPT") may provide another option to provide access to assets.

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2020 Goal 2: Preservation of Access to Assets Transferred to Irrevocable Trusts in 2020

- SLAT/DAPT: Use of DAPTs should not be limited to merely single clients. A DAPT can, for example, be used in combination with a SLAT. For example, one spouse could create a SLAT for the other, and the other spouse could create a DAPT that benefits both the other spouse as well as potentially themselves.
- Hybrid-DAPT: With a hybrid-DAPT the settlor is not named as a beneficiary of the trust initially. Rather a person is granted, in a nonfiduciary capacity, a limited or special POA to add beneficiaries to the trust e.g. a class of potential beneficiaries such as descendants of the settlor's grandparents. IV-B-Pt 1-42

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2020 Goal 2: Preservation of Access to Assets Transferred to Irrevocable Trusts in 2020

- SPAT - A more recent entry to the DAPT-like planning world, developed by Abigail O'Connor, Mitchell Gans and Jonathan Blattmachr, is a special power of appointment trust (SPAT) in which a person in a non-fiduciary capacity is provided a power of appointment to direct the trustee to distribute trust assets to a class of individuals that includes the settlor. The theory of the SPAT is that the trustee has no discretion to make the distribution to the settlor nor is the settlor ever named as a beneficiary, so that therefore a SPAT is not a self-settled trust and, therefore, it should not subject to the jurisprudent that allows creditors access to such a trust. IV-B-Pt 1-42

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2020 Goal 3: Avoiding the Reciprocal Trust Doctrine

- SLAT/Hybrid DAPT POAs - A key to differentiating trusts is the creative use of different powers of appointments in each trust, as will be explained below. For example, if the first spouse creates a spousal lifetime access trust ("SLAT") for the second spouse, that second spouse may create a Special Power of Appointment Trust ("SPAT"), a hybrid–domestic asset protection trust ("Hybrid DAPT"), a traditional DAPT, or perhaps a DAPT that prohibits distributions for 10 years and one day (since Section 548(e) of the US Bankruptcy Code allows the trustee in bankruptcy to access assets in a self-settled trusts created within ten years of bankruptcy in some cases).

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2020 Goal 3: Avoiding the Reciprocal Trust Doctrine

- Different POAs - One spouse's trust could have a limited power of appointment given to somebody, e.g. the beneficiary spouse, that is exercisable during lifetime. The second spouse's trust may only have a testamentary limited power of appointment.
- In the Tax Court's decision in Levy v. Commissioner, the court refused to apply the reciprocal trust doctrine (and the IRS conceded it should not apply) where the trusts the spouses created for each other were identical except the husband granted the wife a presently exercisable broad special power of appointment and she did not create such as power for him. IV-B-Pt 1-47

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2020 Goal 4: Using Irrevocable Trusts to Achieve Basis Step-up

- Achieving a step-up in income tax basis is that the focus of much of current planning. This can be accomplished in the simplest of illustrations by creating a SLAT and giving an elderly and/or perhaps ill senior family member a GPOA over trust assets. The operation of the GPOA will cause the assets of the trust to be included in the powerholder's estate and should therefore qualify those assets for a step up in basis on the death of the powerholder.
- GPOAs could result in adverse unintended consequences such as assets being transferred to an unintended party or an unintentional estate tax. Those risks might be mitigated by carefully crafting or circumscribing the GPOA to mitgate those risks.

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2020 Goal 5: Grantor Versus Non-Grantor Trust Status: How to Choose in 2020 Planning

- POAs can affect structure of each type of trust. Grantor versus non-grantor trust status should consider impact on access in 2020 planning. Discussed Austin Bramwell and Carlyn McCaffrey in Planning with Grantor and Non-Grantor Trusts.
- Grantor Trusts
- POAs in grantor trusts can provide access.
- Power for a person to loan the settlor any amount of assets from the trust without adequate consideration. This can be an invaluable means of accessing assets held in the trust after the transfer has been made.
- The spouse can be named a beneficiary without particular issue.
- If a grantor trust is intended, a DAPT could be used and the settlor could be named a beneficiary and thereby have access to trust assets.

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2020 Goal 5: Grantor Versus Non-Grantor Trust Status: How to Choose in 2020 Planning

- Non-Grantor Trusts. IV-B-Pt 1-8
- Any powers or provisions that could taint the trust is being characterized as a grantor trust would have to expressly be excluded.
- If the non-grantor trust is to be used, a loan provision has to expressly be excluded that would taint the trust as a grantor trust.
- If the spouse of the settlor were named a beneficiary no distributions can be made to that spouse unless approved by an adverse party.
- If a non-grantor trust is to be used, and one of the assets is S corporation stock, then QSST or ESBT provisions would have to be incorporated into the instrument.

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2020 Goal 6: Integrating State Income Tax Planning into 2020 Planning

- Discussed by Recent Developments panel and Jonathan Blattmachr's discussion of Migratory clients.
- POAs can be used to mitigate state income taxation.
- In the Kastner case, the Supreme Court recognized that beneficiary who is a resident of high tax North Carolina and who would have received a distribution of trust assets at a specified age could nullify state income tax avoidance. However, the trust was decanted into a new trust that did not mandate a principal payout at a specified age and thereby avoided that issue. Decanting is a special power of appointment held in a fiduciary capacity.
- IV-B-Pt 1-33

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2020 Goal 6: Integrating State Income Tax Planning into 2020 Planning

- For example, if a trust has a combination of source and non-source income, using a decanting provision or a lifetime limited power of appointment, the trust might be effectively divided and the non-source assets, e.g. marketable securities, moved to a new trust in a no-tax jurisdiction. The decanting could, for example, also remove trustees in the high-tax state that were a factor subjecting the trust to that state's income taxation. This is another illustration of how powers of appointment can be used to achieve state income taxation savings.

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2020 Goal 7: Flexibility Through Creative Uses of Powers of Appointment in 2020 Irrevocable Trusts

- Powers of appointment can infuse flexibility in several ways into the irrevocable trusts being planned for 2020 client transfers. Given the uncertainty of the 2020 election and what might occur with the estate tax system under a Republican versus a Democratic, practitioners should consider incorporating various mechanism to permit flexibility into trusts planned prior to the election. In that way, whatever the outcome of the election, there may be a means of modifying the trust to better meet the client's intended goals.
- Decanting - Incorporating decanting provisions into trust instruments is an example of a right, a special power of appointment, granted to the trustee that can infuse flexibility.
- Lifetime LPOA - A lifetime LPOA could be given to change beneficiaries. This can be used to provide flexibility given the political uncertainties. IV-B-Pt 1-48

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2020 Goal 7: Flexibility Through Creative Uses of Powers of Appointment in 2020 Irrevocable Trusts

- 2038 Power - Consider permitting a named disinterested person, acting in a non-fiduciary capacity, to give the Grantor powers to control the beneficial enjoyment of trust property such that the subject property would thereby become taxable in the Grantor's gross estate under IRC Section 2038. For instance, the Grantor might be given such a Section 2038 power(s) over all or a specific portion of the trust property (or even specific assets) in order to obtain a step-up in basis for appreciated trust property. This type of provision should be addressed in a trust from inception. This is because the power had to have been retained by the settlor, and adding a power later may not be viewed as a power initially retained by the settlor.
- IV-B-Pt 1-37

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2020 Goal 7: Flexibility Through Creative Uses of Powers of Appointment in 2020 Irrevocable Trusts

- LPOA To Direct Trust Distribution To Charity Satisfying 642(c) - For a trust to qualify for a charitable contribution deduction the governing instrument must include the right to distribute to charity. Code Sec. 642(c). For a trust to donate funds to a charity, the trust must meet the governing instrument requirement that it contain authorization to make gifts to charities. If the governing instrument is silent, simply adding charitable beneficiaries through a decanting or non-judicial modification will not satisfy the governing instrument requirement. What about using LPOAs to permit charitable donations? An LPOA that gives the powerholder the right to appoint trust income to charity should suffice to meet the "pursuant to the terms of the governing instrument" requirement.
- IV-B-Pt 1-37

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Special Application of LPOAs – Sharia Inheritance Plan

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Special Application of LPOAs – Sharia Inheritance Plan

- LPOA to Address Sharia Inheritance Plan. IV-B-Pt 1-31
- LPOAs are flexible tools that can be used in creative ways to accomplish a surprising variety of estate and related planning. The following discussion illustrates one such interesting application.
- For many Muslim clients, estate planning is viewed as an act of religious devotion and an attempt to comply with inheritance laws outlined in the Quran. In a famous hadith (statement of the Prophet Muhammad), he said "Do not let two nights pass without writing a will." Islamic Inheritance laws are derived directly from the Quran, primarily from Chapter 4 verses 11, 12, and 176. Shares are non-discretionary.

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Special Application of LPOAs – Sharia Inheritance Plan

- The fractional formulas change depending on which heirs are alive at the moment of death. So a will for a Muslim client can specify that the dispositive provisions shall adhere to Sharia law (perhaps with the exception of the discretionary 1/3rd noted above). The will could also specify what that disposition may be at the date of execution, but that may change before death. Thus, there are several issues that may need to be addressed in administering a Sharia compliant dispositive scheme and an LPOA may be an ideal approach to do so.

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Special Application of LPOAs – Sharia Inheritance Plan

- Another planning concern for Muslim clients is that secular courts are unlikely to have the specialized knowledge.
- Even worse, there have been frequent incidences of anti-Sharia legislation introduced in various states. **Some of this legislation could undermine any faith based provision**. If the jurisdiction in which the client is domiciled had to become involved in interpreting or enforcing a Sharia compliant will, the presence of such legislation could make that impossible
- Instead of relying solely on a will, which may ultimately be subject to probate in a jurisdiction that is hostile to the application of Sharia law, or worse, which may have enacted anti-Sharia legislation (which may have occurred subsequent to the execution of the will), perhaps a better approach to uphold a Sharia compliant estate plan is to use a pour-over will and rely on a funded revocable trust as the primary dispositive document.

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Special Application of LPOAs – Sharia Inheritance Plan

- That trust should include one or mechanisms to effectuate a change in both situs and governing law to a jurisdiction that does not have antagonistic law, e.g. an LPOA to decant. That way a trust can readily be moved from a state that has or may enact legislation that thwarts the Muslim client's wishes to a state that will respect them.
- As part of this Sharia-compliant estate plan, also consider including a Sharia Trust Protector, acting in a non-fiduciary capacity, and granting that person, perhaps a Muslim attorney, Imam or Muslim scholar, to interpret provisions that are Sharia related so that they do not have to be resolved by a secular court. It may also be advisable to go a step further.

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Special Application of LPOAs – Sharia Inheritance Plan

- This measure of flexibility is particular important to carrying out a Sharia complaint estate plan. Consider granting to the Sharia Trust Protector a LPOA to reallocate assets amongst the decedent's Muslim heirs. The determination of whether a particular heir is a "Muslim" and hence to benefit under Sharia law is a matter that should be determined preferably by someone with the appropriate knowledge and expertise in this area of Sharia law, not be a secular court.

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Conclusion and Additional Information

Powers of Appointment a Powerful Planning Tool

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Conclusion

- Powers of Appointment are a Powerful Planning Tool Especially in 2020.

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Additional information

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