

## **Add Estate Planning Flexibility With Powers Of Appointment**

The best laid plans can go awry. Consider the estate plan you may have carefully crafted by taking into account the needs of your family members. After you're gone, events may transpire that you hadn't anticipated or couldn't have reasonably foreseen. For example, a grandchild may suffer a severe disability or creditors may come after your adult child's fortune.

Of course, there's no way of predicting the future, but you can supplement your existing estate plan with a trust provision giving a designated beneficiary a "power of appointment" over some or all of the trust property. Essentially, this person will have the discretion to change distributions from the trust or even add or subtract beneficiaries.

### **Power Of Appointment In Action**

Assuming the holder of this power fulfills the duties properly, he or she can make informed decisions when all the facts are known. This creates more flexibility and adaptability within your estate plan.

Typically, the trust will designate a surviving spouse or an adult child as the holder of the power of appointment. After you die, your surviving spouse has authority to make changes consistent with the language contained in the power of appointment clause. This may include the ability to revise beneficiaries.

For instance, if you give your spouse this power, he or she can later decide if grandchildren are capable of managing property on their own or if property should be transferred to trusts managed by professional trustees. The power of appointment can be used to discourage spending sprees of offspring who haven't demonstrated the ability to handle newfound wealth.

## 2 types of powers

If you take this approach, note there are two types of powers of appointment:

1. ***“General” power of appointment.*** This allows the holder of the power to appoint the property for the benefit of anyone, including him- or herself, his or her estate or the estate’s creditors. The property is usually included in a trust but may be given to the holder outright. Also, this power of appointment can be transferred to another person.
2. ***“Limited” or “special” power of appointment.*** Here, the person holding the power of appointment can give the property to a select group of people who’ve specifically been identified by the deceased. For example, it might provide that a surviving spouse can give property to surviving children, as he or she chooses, but not to anyone else. Thus, this power is more restrictive than a general power of appointment.

Whether you should use a general or limited power of appointment depends on your circumstances and expectations.

## Tax Impacts

The resulting tax impact may also affect the decision to use a general or limited power of appointment. The rules are complicated, but property subject to a general power of appointment is typically included in the taxable estate of the designated holder of the power. However, property included in the deceased’s estate receives a step-up in basis to fair market value on the date of death. Therefore, your heirs can sell property that was covered by a general power of appointment with little or no income tax consequences.

In contrast, property covered by a limited power isn’t included in the holder’s estate. However, the new heirs inherit the property with a carryover basis and no step-up in basis. So, if the heirs sell appreciated property, they face a potentially high capital gains tax.

This requires an in-depth analysis by your estate tax advisor. But remember that property subject to estate tax can be sheltered by the federal gift and estate tax exemption. Currently, the exemption is \$10 million (indexed to \$11.7 million for 2021) but is scheduled to revert to \$5 million after 2025. If estate tax isn't a concern, a general power of appointment may be preferable.

Conversely, a limited power of appointment may be used if capital gains will be relatively small or postponed indefinitely. This may be the case for, let's say, a seaside cottage that has remained in the family for generations.

### **A Word Of Caution**

Be aware that even though a power of appointment has advantages, it isn't for everyone. Consult with your estate planning advisor to determine if adding a power of appointment is right for you.

© 2021



1875 Century Park East, Suite 2000  
Los Angeles, CA 90067  
(P) 310 553-8844 | (F) 310 553-5165  
[www.weinstocklaw.com](http://www.weinstocklaw.com)