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# General Powers of Appointment: The Ones to Watch

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# General Powers of Appointment: The Ones to Watch

-by Neil E. Harl*

The last step in drafting a will or trust is to scan the document or documents to see if a general power of appointment lurks within that could cause unpleasant surprises at death.[1] A general power of appointment, in contrast to a special power of appointment, is one that can be exercised by the person to whom it was given in favor of that individual, that individual's estate, the creditors of that individual or the creditors of that individual's estate.[2] In other words, the holder of a general power of appointment can benefit from the exercise of the power.

A special power of appointment, by contrast, can be exercised to benefit anyone in the whole wide world except for those listed as giving rise to a general power of appointment.

**An important exception**

A power to consumer, invade or appropriate property for the benefit of the decedent *which is limited by an ascertainable standard* (health, education, support or maintenance) is not considered a general power of appointment.[3]

**If an unwanted general power of appointment is discovered after execution of the documents**

The discovery of a general power of appointment after execution of the will or trust can pose significant planning problems for the holder of the power. Frequently, it involves unintended powers granted to the trustee or other fiduciary. Fortunately, there is a solution to the problem. The Internal Revenue Code provides a solution to such a dilemma.[4] An attempt to eliminate the potential impact of such a general power can result in a *gift* which may be objectionable.

However, a power of appointment in favor of a person other than the grantor, which has been renounced or disclaimed within a reasonable time after becoming aware of its existence, is not treated as a gift.[5] The disclaimer or renunciation is not treated as a release of the power.[6] That can be a useful solution.

The document of renunciation or disclaimer should be dated and executed promptly and filed in a secure place. The document is not required to be filed publicly.

**The 5/5 power and powers of appointment**

A non-cumulative right to withdraw the greater of five percent or $5,000 from the

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trust principal each year typically from the bypass trust (generally referred to as the 5/5 power), may result in inclusion in the gross estate to the extent of the value of rights that had not lapsed. Lapses of a 5/5 power do not result in either federal gift tax or federal estate tax *as to the value of the lapsed property before the year of death*.[7]

However, for the year of death, there is included in the gross estate the amount which the holder of the power was entitled to withdraw for the year in which death occurred, less any sums were or might have been received during the time in that year in which the individual was living.[8] Thus, the only concern at death is the amount of unexercised value in that year. As the regulations state,[9] –

> ". . . at death. . . there will be included in his gross estate the [amount] which he was entitled to withdraw for the year in which his death occurs less any amount which he may have taken during the year."

The lapses in prior years *are not included in the gross estate*. But the "annual exemption" of the 5/5 power does not apply to the withdrawals not made for the year of death. As some have suggested, this might encourage drafters to make the power exercisable only for a certain period each year, such as the last two weeks of the year. The authority for that, however, is sparse.

**ENDNOTES**

[1] See I.R.C. § 2041(b)(1). See generally 5 Harl, *Agricultural Law* § 43.02[7][c] (2016); Harl, *Agricultural Law Manual* § 5.02[6] (2016).

[2] I.R.C. § 2041(b)(1).

[3] E.g., Forsee v. United States, 76 F. Supp. 2d 1135 (D. Kan. 1999) (right to invade corpus for "happiness" was not limited by an ascertainable standard; corpus of trust included in the gross estate). See Ltr. Rul. 9344004, July 13, 1993 ("health, maintenance support, comfort, and welfare" not limited by an ascertainable standard).

[4] I.R.C. § 678(d).

[5] I.R.C. § 678(d). See Ewing v. Roundtree, 228 F. Supp. 132, 143 (M.D. Tenn. 1964).

[6] *Id*.

[7] Treas. Reg. § 20.2041-3(d)(3).

[8] See Estate of Dietz v. Comm'r, T.C. Memo. 1996-471. See also Ltr. Rul. 201216034, Jan. 11, 2012; Ltr. Rul. 201038004, June 15, 2010.

[9] Treas. Reg. § 20.2041-3(d)(3).

# CASES, REGULATIONS AND STATUTES

by Robert P. Achenbach, Jr

## BANKRUPTCY

### GENERAL

**AUTOMATIC STAY**. The debtor was a nursery owner who entered into a "contract grow agreement," under which a creditor supplied trees to be grown by the debtor. The agreement provided that the creditor would supply much of the cost of raising the trees to market condition and would purchase the trees back from the debtor at a cost less than market value and decreased by the amounts provided for the raising costs. Under one provision of the agreement, the debtor waived any right to the automatic stay as to any claim filed by the credit in a bankruptcy proceeding. The creditor sought relief from the automatic stay under two theories: (1) the waiver of the right to the automatic stay and (2) its characterization of the agreement as a bailment such that the trees were not bankruptcy estate property because, under the agreement, the creditor retained title to the trees. The court first noted that waivers of rights to automatic stays are general held to be unenforceable as against public policy. In addition, the court found that (1) the waiver was not bargained for and was not exchanged for any consideration, (2) the debtor had a reasonable chance for a successful reorganization which would be threatened by allowing relief from the automatic stay, and (3) relief from the automatic stay would harm other creditors' rights. Thus, the court held that relief from the automatic stay would not be granted merely because of the waiver provision in the grower's agreement. ***In re* Jeff Benfield Nursery, Inc., 2017 Bankr. LEXIS 196 (Bankr. W.D. N.C. 2017)**.

## FEDERAL FARM PROGRAMS

**FARM PROGRAM PAYMENT LIMITATION**. The plaintiff was a farmer who had received federal farm program payments in 2005 through 2008. The FSA determined that the plaintiff was not a separate person from an LLC which also received payments. The FSA sought the return of all payments received by the plaintiff. The court noted that the plaintiff had exchanged undocumented loans to and from the LLC and made bulk purchases of farm supplies with the LLC such that it was impossible to determine which assets and liabilities belonged to the plaintiff or LLC. Therefore, the plaintiff was not a separate person for purposes of the payment limitations. The plaintiff also argued that the payments received by the plaintiff and the LLC did not exceed the per person payment limitation; therefore, no refunds were necessary. The court held that, because the plaintiff was not a separate person from the LLC, separate payments to the