HG&G UPDATE

Hofheimer Gartlir & Gross, LLP Spring 2003

The *Power* of a Power of Attorney

You have the power to name someone who could manage your assets for you if you were to become disabled and consequently unable to act for yourself. Many people mistakenly believe that in case they become disabled, a spouse, parent, child or other family member or significant other can act for them. Neither a family relationship nor a close friendship confers any power to manage your assets; there must be other formal legal authority.

Formal legal authority is required before someone can manage financial assets for another.

Many people incorrectly assume that one joint owner can handle any transaction regarding jointly held assets. Generally, both owners' signatures are required to sell, mortgage or otherwise deal with joint assets, except bank accounts.

One of the more serious financial problems that can result from one's disability is the inability to file tax returns and to deal with the Internal Revenue Service and other taxing authorities. Expensive penalties and non-deductible interest charges can be imposed for filing returns late or for failing to file them at all.

A general power of attorney can avoid many of the financial problems caused by disability.

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Without a power of attorney or a revocable trust, these problems usually can be resolved only through an expensive and embarrassing court proceeding for the appointment of a guardian.

The general power of attorney is a powerful, as well as a dangerous, document. It allows someone to act as your legal alter-ego. That person can perform almost every act that you can perform and can legally bind you by his or her actions. The person whom you choose to act for you is called an "attorney-in-fact," but need not be a lawyer. You may choose only one person to act for you, or you may choose several people.

Acting as an attorney-in-fact carries with it the potential for personal liability for acting inappropriately or for not acting. Before naming someone as attorney-in-fact, it is prudent to ask them whether they will accept this responsibility. It is also reasonable to ask whether that person would expect to be compensated for acting as attorney-in-fact.

Banks, brokers and others are often reluctant to honor powers of attorney. To encourage them to act on the instructions of the attorney-in-fact, they need to be assured that they can rely on the effectiveness of the power of attorney. Since a power of attorney is no longer valid after one's death, banks, brokers and others usually insist on obtaining evidence that the person who signed the

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power of attorney is alive, before they recognize the attorney-in-fact's authority.

You can revoke a power of attorney merely by notifying the attorney-in-fact that you have terminated his or her authority. But a dishonest attorney-in-fact could fail to notify banks, brokers or others that you have terminated the power. You might not know to whom copies of your power of attorney have been furnished. Then, you would need to notify everyone with whom you deal that you have revoked your power of attorney. You may conclude that these risks are not as serious as the risks of not having a power of attorney.

A gift made while the donor is disabled may fail, if no specific authority is provided in the power of attorney.

The Internal Revenue Manual–Audit advises IRS attorneys that without specific authority in it, a power of attorney does not permit making gifts of your assets. If you were disabled, an attempt to make gifts of your assets, without specific authority, could result in the failure of the gift. The value of the assets that were attempted to be given away would be included in your estate. In some cases, the recipient of the attempted gift could be held to have received taxable income rather than a gift. But you may allow your attorney-in-fact to make gifts of your assets to people you select now. A non-tax reason for making gifts is to continue your practice of helping to support relatives and close friends. The primary tax reasons to do this are to minimize your income tax, your potential estate tax and the additional 49% generation-skipping tax. These gifts should ordinarily not exceed the $11,000 per person annual Federal gift tax exclusion.

It is generally not recommended to permit the attorney-in-fact to make substantial gifts of your assets, assets that you may feel should be conserved for your future needs. To the extent that the gifts exceed the annual Federal gift tax exclusions, their value is added back to the value of your estate for estate tax purposes. Allowing the attorney-in-fact to make substantial gifts to himself or herself can create additional tax hazards at the death of the attorney-in-fact or yourself. Additionally, allowing the attorney-in-fact to make substantial gifts of your assets to himself or herself may subject your own assets to claims of the creditors of the attorney-in-fact.

You can also allow your attorney-in-fact to expend your assets for tuition and medical expenses for others whom you now name or designate. There is no requirement in the Internal Revenue Code that tuition payments and medical expenses may be paid only for family members. The amounts that your attorney-in-fact can expend for tuition and medical expenses each year can be either limited or unlimited, as you choose. Tuition payments can be made for anyone at an educational organization if paid directly to the organization. Medical expenses can be paid for all medical expenses paid directly to the provider, including medical insurance premiums. Any amount expended for these purposes is removed from your taxable estate and is also free of both the gift tax and the additional 49% generation-skipping tax.

You may give your attorney-in-fact the power to disclaim any assets that you may receive or inherit. A properly planned disclaimer can permit assets to pass to others whom you might want to benefit. Besides, a properly planned disclaimer can minimize your potential income, gift, estate and generation-skipping taxes. However, your attorney-in-fact will need to determine whether allowable tax credits may dictate against disclaiming assets.

If you desire, you can authorize your attorney-in-fact to make charitable contributions of your assets either to charities that you select or to charities that your

attorney-in-fact selects. You can impose a maximum limit on the amount that may be given to each charity each year. Alternatively, you may impose a maximum limit on the aggregate amount that may be given to all charities each year. If you desire, you can permit your attorney-in-fact to make unlimited charitable gifts. This can continue your practice of making charitable gifts and can qualify for income tax deductions, as well as removing assets from your gross estate.

Please understand that you will retain complete control over your assets as long as you have the capacity to do so. You can also change or revoke the power of attorney at any time while you have the capacity to do so.

In selecting your attorney-in-fact, integrity is the most important criterion. Many people designate the person whom they have chosen to be executor to act as the attorney-in-fact. Financial ability and experience are secondary. If you name only one person to act alone, he or she might not be available when needed, because of absence, disability or death. If you feel strongly that only one person can exercise these heavy responsibilities properly, you can name that person alone, recognizing his or her own vulnerability to death, absence and disability.

Naming a substitute attorney-in-fact, who could act only if the original attorney-in-fact dies or becomes disabled, is another possibility. However, requiring a determination that the initial attorney-in-fact is unable to act may delay or hinder the substitute's ability to act.

If you initially name two or more people to act together, you could allow each of them to act independently, or you could require them to act together. If you require them to act together, and if one or more of them is unavailable, a bank, broker or other institution may not comply with the instructions of the other acting alone. If you name more than two people to act together, you may allow them to act by majority vote. You should not give one attorney-in-fact the power to overrule another. If the person with the power to overrule the others is unavailable, no bank, broker or other institution will be able to act on the instructions of the others, for fear that they will be overruled later. There would not seem to be any point in naming one attorney-in-fact who could be overruled by another.

You can make the power of attorney effective as soon as you sign it. That would permit your attorney-in-fact to act, even if you were physically present and in good health. You may want to ignore the possibility that the person or persons you choose could violate your trust in them. Alternatively, you could provide that the power of attorney would become effective only when someone whom you now select certifies that you have become disabled or otherwise unavailable. Until that certification is made, the power of attorney would be useless. The questions then arise, how to define disability, whether a physician would be willing to certify that you have become disabled, and whether that certification will satisfy banks, brokers and others.

Depending upon your confidence in the judgment and integrity of your attorney-in-fact, you may want to furnish him or her and any substitutes with copies of the power of attorney as soon as you sign it. If you have the slightest reservation about this, you may wish to advise your attorney-in-fact that all of the copies of the power of attorney are in someone else's custody. If the circumstance arises when the power of attorney is needed, copies can be obtained by satisfying that other person that the need to use the power

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of attorney has arisen. Only then would the attorney-in-fact be able to establish his or her authority to act. However, if the attorney-in-fact feels that there is great urgency in acting, requiring him or her to go through this procedure may be counter-productive.

There is relatively little that one can do to avoid disability that happens because of so many different causes. What one can do is to provide for the intelligent and safe management of one's assets if disability strikes. That is the function of the general power of attorney.

For more information, please call Ed Schlesinger or one of the other partners at the firm.

Pre-Mortem Estate Planning Checklist

The Second Edition of *Pre-Mortem Estate Planning Checklist* authored by our partner Ed Schlesinger and co-authored by our partner Bob Howard has just been published by ALI-ABA, American Law Institute-American Bar Association. This volume includes discussions of the significant changes made to the estate, gift and generation-skipping transfer taxes made by the Economic Growth and Tax Relief Reconciliation Act of 2001, estate tax issues concerning insurance, powers of attorney and one hundred tips on long-term trusts.

Long Island Office

We are pleased to announce the relocation of our Long Island Office to 1010 Northern Boulevard, Great Neck, New York 11021.

The telephone number is 516-336-2592. The fax number is 516-336-2591.

Gary B. Sachs will continue to practice at both our New York and Long Island offices.

New Telephone Numbers

We have a new general telephone number, 212-944-0500, in addition to our old number, 212-818-9000. Our new general fax number is 212-869-4930.

Our attorneys continue to have their direct dial telephone numbers as well as their direct dial fax numbers.

Visit us on our website: www.hgg.com

About Hofheimer Gartlir & Gross, LLP

The firm conducts a general commercial practice. Our principal practice areas are:

- real estate
- corporate and securities law
- general business and commercial law
- cooperative and condominium matters
- financial institutions (loan transactions, leasing, acquisitions, credit restructuring, workouts, foreclosures)
- estate planning
- trust and estate administration
- general litigation and alternate dispute resolution
- matrimonial and family law
- taxation
- bankruptcy and creditors' rights

Clients of the firm range from major financial institutions and public corporations to closely-held businesses, individuals and families.

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HG&G Update is written and published by Hofheimer Gartlir & Gross, LLP, 530 Fifth Avenue, New York, New York 10036, (212) 818-9000.

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