License to Steal: Implied Gift-Giving Authority and Powers of Attorney

Hans A. Lapping

Attorneys of elderly clients are often called upon to draft a power of attorney to handle an elderly client's estate plans. The general powers conferred by the power of attorney allow the attorney-in-fact to act in lieu of the principal. In addition to the power of attorney, a program of estate reduction is commonly implemented by making annual gifts of $10,000 applicable to the gift tax exclusion. The Internal Revenue Service holds the position that an attorney-in-fact who makes such gifts on behalf of the elderly client is actually making a "revocable transfer" which is not entitled to the gift tax exclusion but is to be included in the decedent's estate.

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I. Introduction

In 1990, there were over 31.2 million Americans age sixty-five or older, and this population is expected to exceed 34.8 million by the year 2000.[1] As America ages, more people are realizing that they may some day need assistance with their financial affairs should they become incapacitated.[2] Consequently, attorneys are increasingly being

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1. Bureau of the Census, U.S. Dep't of Commerce, Series P23-178, Sixty-Five Plus in America, Highlights 2-3, tbl. 2-1 (1992) [hereinafter Sixty-Five Plus in America] (in 1960 there were 16 million persons aged 65 or older and 20 million in 1970).

2. That the elderly as a group have substantial financial assets is evidenced by the fact that roughly 70% of the wealth in the United States can be attributed to the elderly. *See* Sixty-Five Plus in America, *supra* note 1, at 4-18, 4-21. Furthermore, almost 75% of older Americans own their own homes (most mortgage free)

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I. Introduction

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called upon by their clients to draft powers of attorney[3] as part of the elderly person's estate plans. Often these general powers authorize the attorney-in-fact to do everything the principal could do if personally present and capable of acting.[4]

In addition to the implementation of a power-of-attorney, prudent estate planning frequently involves a program of estate reduction by making gifts within the limit of the annual $10,000 per donee gift

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and many have discretionary income. *See* BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, SERIES P-70, NO. 7, HOUSEHOLD WEALTH AND ASSET OWNERSHIP: 1984 (1986).

3. A power of attorney is a simple document whereby the principal can nominate another person as an attorney-in-fact or agent to act on behalf of the principal. The attorney-in-fact can then generally manage the assets and affairs of the principal. The use of this technique is unavailable, however, in planning for a presently mentally incapacitated individual because the power of attorney will not be valid if the person executing it does not possess the requisite capacity to understand the nature and significance of the consequences of his or her act.

A power of attorney may be general, special, limited, or a combination of any of these forms. A general power of attorney is an unlimited power that gives an agent broad powers, e.g., to do anything the principal could do. A special power of attorney is a very specific grant of authority, e.g., to sell a particular stock to a particular buyer at a particular price. A limited power is a general power with limitations, such as the authority to sell a particular stock to any purchaser at a particular price. A limited power can restrict the type or transaction the agent is authorized to undertake or can limit the period of time for which the power will be effective.

Because a power of attorney is premised on an agency relationship, a power of attorney automatically terminates upon the death of the principal. The agency relationship also terminates if the agent becomes incapacitated or dies. The power of attorney itself also can provide for a specific time limit or event that triggers its termination.

A nondurable power of attorney, usually referred to as a simple power of attorney, unlike a durable power of attorney, automatically terminates upon disability or incompetency of the principal. Because the nondurable power of attorney ceases to be in effect when it is most desperately needed, i.e., upon the disability or incompetency, lawmakers have recognized the need for a durable power of attorney to survive the principal's disability or incompetency.

Where durable powers are permitted, the powers can survive the principal's incapacity (but still terminate on the principal's death) and, therefore, can be relied upon for extended management of the principal's affairs. All 50 states and the District of Columbia recognize durable powers of attorneys. The advent of the durable power of attorney solved a major shortcoming of powers because a durable power survives disability or incapacity and provides an informal and inexpensive alternative to the appointment of a committee, conservator, or guardian. *See* Michael S. Insel, *Durable Power Can Alleviate Effects of Client's Incapacity*, 22 EST. PLAN. 37, 37 (1995); *see also* FRANCIS J. COLLIN ET AL., DURABLE POWERS OF ATTORNEY AND HEATH CARE DIRECTIVES § 1.01-1.02; 3 AM. JUR. 2D *Agency* §§ 23-35 (1986).

4. Although the actual words may vary from jurisdiction to jurisdiction, a typical power of attorney might vest an attorney-in-fact with powers "to do and perform all and every act which I as an owner of said property could do or perform and I hereby ratify and confirm all that my attorney in fact shall do or cause to be done under this durable power of attorney." DENIS CLIFFORD, THE POWER OF ATTORNEY BOOK, Form 1 (1990).

tax exclusion. This gift-giving technique used in estate planning is common and is contemplated by the Internal Revenue Code (Code).[5]

Because these two approaches to estate planning often intersect, it becomes advisable for an attorney-in-fact to make gifts of the principal's assets by taking advantage of the annual gift tax exclusion. Despite the fact that a general grant of power-of-attorney would seemingly include the ability to make gifts, the Internal Revenue Service (IRS or Service) has consistently challenged the authority of those attorneys-in-fact who attempt to make gifts[6] by arguing that the agents are acting *ultra vires*.[7] According to the IRS, because the attorney-in-fact is acting without authority, the gifts are actually "revocable transfers" and, consequently, are includable in the decedent's estate. Although most courts have agreed with the IRS's position, several recent Tax Court and court of appeals decisions have interpreted broad grants of power to include the authority to make gifts. Furthermore, both Alabama[8] and Virginia[9] have enacted legislation that specifically recognizes that a general grant of power to an attor-

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5. Metzger v. Commissioner, 38 F.3d 118 (4th Cir. 1994).

6. *Agents Under Powers of Attorney: Can They Make Gifts?*, 19 TAX MGMT. EST., GIFTS & TR. J. 89, 89 (1994).

7. If an action is *ultra vires*, it is an act performed without any authority to act on the subject. *See* BLACK'S LAW DICTIONARY 1522 (6th ed. 1990).

8. ALA. CODE § 26-1-2.1 (Michie Supp. 1994). The code provision, which became effective May 6, 1994, reads in its entirety:

> Gifts by power of attorney:
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> (a) If any power of attorney or other writing either authorizes an attorney in fact or other agent to do, execute, or perform any act that the principal might or could do, or evidences the principal's intent to give the attorney in fact or agent full power to handle the principal's affairs or deal with the principal's property, the attorney in fact shall have the power and authority to make gifts of any of the principal's property to any individuals, including the attorney in fact or agent, within the limits of the annual exclusion as provided by Section 2503(b) of Title 26 of the United States Code, and taking into account the availability of Section 2513 of Title 26 of the United States Code, as the same may from time to time be amended, or to organizations described in Sections 170(c) and 2522(a) of Title 26 of the United States Code, or corresponding future provisions of federal tax law, or both, as the attorney in fact or agent shall determine: (1) to be in the principal's best interest; (2) to be in the best interest of the principal's estate; or (3) that will reduce the estate tax payable on the principal's death; and is in accordance with the principal's personal history of making or joining in the making of lifetime gifts.
>
> (b) Subsection (a) shall not in any way impair the right or power of any principal, by express words in the power of attorney or other writing, to further authorize, expand, or limit the authority of any attorney in fact or other agent to make gifts of the principal's property.

ney-in-fact includes implied authority to make gifts, thereby denying the IRS the ability to challenge powers-of-attorney on this ground in these two states.[10]

This note will review the IRS's position with regard to the gift-giving powers of agents, examine those rulings that have interpreted a general grant of power to include gift-giving authority, and scrutinize the recently enacted laws of Virginia and Alabama. Furthermore, this note will propose that Virginia and Alabama should strongly consider repealing their new statutes because the statutes create the potential for fraudulent and abusive uses of the general powers-of-attorney after a principal becomes incapacitated.

> (c) This section is declaratory of Section 26-1-2 and shall not be construed to nullify any actions taken by any attorney in fact prior to May 6, 1994.

9. VA. CODE ANN. § 11-9.5 (Michie 1993). The Virginia provision reads as follows:

> Gifts under power of attorney
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> A. If any power of attorney or other writing (i) authorizes an attorney-in-fact or other agent to do, execute, or perform any act that the principal might or could do or (ii) evidences the principal's intent to give the attorney-in-fact or agent full power to handle the principal's affairs or deal with the principal's property, the attorney-in-fact or agent shall have the power and authority to make gifts in any amount of any of the principal's property to any individuals or organizations described in sections 170(c) and 2533(a) of the Internal Revenue Code or corresponding future provisions of federal tax law, or both, in accordance with the principal's personal history of making or joining in the making of lifetime gifts.
>
> B. Subsection A shall not in any way impair the right or power of any principal, by express words in the power of attorney or other writing, to authorize, or limit the authority of, any attorney-in-fact or other agent to make gifts of the principal's property.
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> C. After reasonable notice to the principal, an attorney-in-fact or other agent acting under a durable general power of attorney or other writing may petition the circuit court for authority to make gifts of the principal's property to the extent not inconsistent with the express terms of the power of attorney or other writing. The Court shall determine the amounts, recipients and proportions of any gifts of the principal's property after considering all relevant factors including, without limitation, (i) the size of the principal's estate, (ii) the principal's foreseeable obligations and maintenance needs, (iii) the principal's personal history of making, or joining in the making of, lifetime gifts, (iv) the principal's estate plan, and (v) the tax effects of the gifts.

10. Under the law of agency, a power of attorney is interpreted according to the laws of the state in which it is executed. Consequently, if a power is executed in Virginia or Alabama and does not explicitly grant a power to make gifts, the IRS is unable to challenge any gift-giving activities on the agent's part because the law in those states recognizes an implicit right to make gifts in a broad grant of power. *See* 3 AM. JUR. 2D *Agency* § 23 (1986).

II. Background

Before examining the various arguments offered by the Internal Revenue Service, the courts, and the states that have included implied gift giving power in their power of attorney statutes, it is necessary to undertake a brief discussion of the gift and estate taxes.

A. The Gift Tax

The gift tax is a tax on the gratuitous transfer of property that is computed and collected annually.[11] In 1976, the separate gift and estate taxes were unified into one structure. Gift taxes payable on gifts made after 1976 are computed essentially in the same manner as they were for gifts prior to that date; however, the rate schedule applied is the estate tax rate schedule.[12]

Although "gift" is not defined in the Internal Revenue Code of 1986, as amended, section 2512(b) of the Code provides for valuation of gifts in accordance with the transfer of property for "an adequate and full consideration in money or money's worth,"[13] with the difference being the amount of the gift. The gift tax only applies to transfers by individuals, but a transfer by a corporation may be attributed to individual shareholders,[14] and a transfer by an incompetent's guardian, properly authorized, is treated as a transfer by the incompetent.[15]

For the purposes of this note, the most important aspect of the gift tax is the annual $10,000 exclusion per donee that is provided for in section 2503(b). According to the Code, a donor can give up to

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11. RICHARD B. STEPHENS ET AL., FEDERAL ESTATE AND GIFT TAXATION ¶ 9.03[3] (1991).

12. *Id.* ¶ 1.03[1]. The estate and gift taxes were unified by the Tax Reform Act of 1976 in order to curtail the potential estate tax savings offered by lifetime gifts. Among the advantages prior to the merger were that the gift tax rate was 25% lower than the estate tax rates. A separate lifetime exemption of $30,000 was allowed for gift tax purposes. Lifetime gifts were not taken into account in determining the donor's estate tax bracket unless the gift was includable in the decedent's gross estate, and the gift taxes on lifetime gifts were not included in the donor's gross estate, even if the gift itself was so included.

13. I.R.C. § 2512(b) (1989).

14. Treas. Reg. § 25.2511-1(h)(1) (1995).

15. *See* Commissioner v. Greene, 119 F.2d 383 (9th Cir. 1941), *cert. denied*, 314 U.S. 641 (1941); Rev. Rul. 67-280, 1967-2 C.B. 349. As will be seen below, lifetime gifts made by an attorney-in-fact under a power of attorney from the decedent which did not expressly confer the power to make gifts were, under state law, revocable transfers and thereby includible in the decedent's estate, even though the transfers would have been gifts for gift tax purposes. Estate of Casey v. Commissioner, 949 F.2d 895 (4th Cir. 1991).

$10,000 to an unlimited number of recipients during any calendar year without the gifts being subject to any gift tax.[16] Assuming the gifts are properly executed, the purpose of the exclusion is to obviate the need for the record keeping of "small gifts," but it has also proven to be an effective estate tax planning tool because the $10,000 gifts are not includable in the donor's gross estate.[17] To qualify for the annual exclusion, the gift must be a transfer of a present interest in property rather than a future interest[18] and be completed within the calendar year.[19]

In light of the exclusion set out in section 2503(b), tax planners have encouraged financially secure clients to engage in an aggressive strategy of making annual gifts so that they may ultimately reduce the value of their gross estate, thereby reducing the amount of taxes due upon death.[20] This strategy often gives rise to circumstances whereby an attorney-in-fact seeks to ensure that the principal is able to take advantage of the tax break. However, because this election includes the likelihood of avoiding estate taxes, the IRS has argued that they are invalid.

B. The Estate Tax

To fully understand the position that the Service has taken with regard to gifts made by attorneys-in-fact operating under a power of

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16. I.R.C. § 2503(b).

17. *See* STEPHENS ET AL., *supra* note 11, ¶ 9.04[1][a].

18. Under Reg. 25.2503-3(a), a future interest includes reversions, remainders, and other interests or estates (vested or contingent), and regardless of whether they are supported by a particular interest or estate, that will commence in use, possession, or enjoyment in the future. Gifts placed in trust in which the ultimate beneficiary cannot obtain the benefit until some future time generally do not meet the present interests requirement. *See* STEPHENS ET AL., *supra* note 11, ¶ 9.04[3][a].

19. The IRS has taken a hard-line approach when it comes to completing the gift within the calendar year. In fact, many taxpayers who wait until the end of the year to make their annual gifts run the risk of disqualifying the gifts in the year in which they were intended because there is no carryover for an unused annual gift tax exclusion. This is especially true with some types of property such as real estate and partnership interests in that they may require time for the transfer to be completed. Even a gift of money, if by check, may be questioned by the Service when the checks do not clear the donor's bank in the year for which they are intended to take effect. *See* Metzger v. Commissioner, 38 F.3d 118 (4th Cir. 1994).

20. For example, assume that a taxpayer has a gross estate valued at $1 million dollars, $250,000 of which is in the form of cash. Suppose further that that taxpayer has one child, *B*, to whom the taxpayer wants the entire estate to pass upon death. By taking advantage of the gift tax exclusion, the taxpayer can give *B* up to $10,000 free of any taxes each year. Therefore, over the course of 10 years, the taxpayer could transfer up to $100,000 tax free whereas if the taxpayer waited until death, the $100,000 made in gifts would be included in the gross estate and taxed by the federal government before *B* received any money.

attorney, it is necessary to understand how to determine the decedent's gross estate.[21] Code section 2031 defines the "gross estate" to include the value of all property real or personal, tangible or intangible, to the extent provided by sections 2033 through 2046.[22] For the purposes of this note, only three sections are of importance, sections 2033, 2035, and 2038.

The basic gross estate provision, section 2031, requires all property in which the decedent had an interest at the time of death to be included in the decedent's gross estate.[23] The nature of the property or the use to which it was put during the decedent-owner's lifetime has no significance as far as the tax is concerned. Thus, personal effects, stocks, bonds, furniture, jewelry, works of art, bank accounts, and interests in businesses conducted as sole proprietorships and partnerships are all included in the deceased's gross estate.[24]

Code section 2035 provides that any adjustments which decrease the overall worth of the estate due to gifts made within three years of death are to be included in the value of the gross estate. Previously, all taxable gifts made within three years of death were included in the donor's gross estate unless it could be shown that the gifts were not made in contemplation of death.[25] This rule was designed to preclude tax avoidance because the gift tax and estate tax rates were separate and the former was lower than the latter.[26] When the gift and estate tax rates were combined into the unified transfer tax, the reason for the rule regarding gifts in contemplation of death largely disappeared.[27] However, the three-year rule has been retained for the following items: (1) any gift tax paid on gifts made within three years of

21. The federal estate tax is imposed by § 2001(a) of the Internal Revenue Code on the transfer of the taxable estate of every decedent who is either a citizen or a resident of the United States. I.R.C. § 2001(a) (1989). Six principal steps determine federal estate tax liability. First, the gross estate is determined under I.R.C. §§ 2031-2046. Next, the taxable estate is determined by subtracting from the gross estate the deductions permitted under §§ 2051-2056. Adjusted taxable gifts are then determined and added to the taxable estate. To that sum, the estate tax rates found in § 2001 are applied to determine a tentative tax. From that tax figure, an amount for the gift tax on post-1976 gifts is subtracted to determine the gross estate tax. Finally, credits against the tax allowed by §§ 2010-2016 are subtracted from the tax to determine the actual liability of the estate, the net estate tax payable. *See* Treas. Reg. § 20.0-2(b)(1)-(5) (as amended in 1992).
22. I.R.C. § 2031.
23. I.R.C. § 2033.
24. STEPHENS ET AL., *supra* note 11, ¶ 4.02.
25. *Id.* ¶ 4.07[1].
26. *Id.* ¶ 4.07[1]-[2].
27. *Id.*

death, and (2) any property interests transferred by gift within three years of death that would have been included in the gross estate by virtue of the application of section 2036 (transfers made within a retained life estate), section 2037 (transfers taking effect at death), section 2038 (revocable transfers), and section 2042 (proceeds of life insurance).[28]

Code section 2038, along with sections 2036 and 2037, was enacted on the premise that the estate tax can be avoided on lifetime transfers only if the decedent does not retain control over the property. The logic of this approach seems difficult to dispute. One should not escape the tax consequences of property transfers at death while remaining in a position during life to enjoy some or all of the fruits of ownership.[29] Under section 2038, the gross estate includes the value of property interests transferred by the decedent (except to the extent that the transfer was made for full consideration) if the enjoyment of the property was subject, at the date of the decedent's death, to any power of the decedent to *alter, amend, revoke, or terminate* the transfer. This includes the power to change the beneficiaries of the power to accelerate or increase any beneficiary's enjoyment of the property.[30]

The capacity in which the decedent could exercise the power is immaterial. If the decedent gave property in trust, making him or herself the trustee with the power to revoke the trust, the property is included in his or her gross estate.[31] If the decedent named another person as trustee, with the power to revoke, but reserved the power to later appoint him or herself trustee, the property is also included in his or her gross estate.[32] If, however, the power to alter, amend, revoke, or terminate was held at all times solely by a person other than the decedent and the decedent did not reserve a right to assume these powers, the property is not included in the decedent's gross estate.[33]

The Internal Revenue Service has used these code provisions to oppose gifts made by attorneys-in-fact. The IRS argues that the agents

28. *Id.* ¶ 4.07[2][d]. This section is of utmost importance to the discussion because the IRS classifies gifts made by an attorney-in-fact as "revocable transfers" under the provisions of § 2038 and, hence, these gifts are included in the gross estate of the decedent. *Id.*

29. *Id.* ¶ 4.08.

30. *Id.* ¶ 4.10[2].

31. *Id.*

32. *Id.*

33. *Id.* ¶ 4.10[4][a-g].

are acting without authority to gratuitously transfer the principal's property and, therefore, the gifts are actually "revocable transfers" which can be included in the decedent's gross estate.

III. Analysis

A. The Argument of the IRS

One of the Service's first technical advice memorandums[34] on the issue of whether or not an attorney-in-fact can make gifts of the principal's property was issued in 1981 and was not hostile to the arrangement under the specific facts of the case. According to the memo, *A* executed and gave *B* a New York Statutory Short Form Power of Attorney during June of 1975. As *A*'s agent, *B* made gifts of *A*'s property to their children and grandchildren in 1975, 1976, 1977, and 1978 in the form of stocks and cash. Gift tax returns were filed for the gifts made in 1975 and 1976. *A* died on December 20, 1978, and the gifts made in 1975 and 1976 were excluded from his gross estate. *B* was appointed executor of *A*'s estate and filed the estate tax return and gift tax returns for the 1977 and 1978 gifts.[35]

The estate auditor argued that the New York Statutory Short Form Power of Attorney did not expressly state that the agent may transfer the principal's property by gift.[36] Accordingly, the auditor wanted to include in *A*'s gross estate, under sections 2033 and 2038 of the Code, all the decedent's property that *B* transferred to his children and grandchildren when *A* was alive.[37] *B* countered by arguing that the transfers she made were done as part of a documented plan beginning in 1968 to give the children and grandchildren a thousand shares of company *C* for ten years at the rate of a hundred shares per year.[38] *B* argued further that the gifts of cash at Christmas to the grandchildren of *A* continued *A*'s past practice of making cash gifts to take advantage of the annual gift tax exclusion and to provide for their

34. A Technical Advice Memorandum (TAM) is a request for assistance by a local office of the IRS and typically arises during an audit. The TAM is issued by the National Office of the IRS and is not binding on the Service. *See also* KEVIN E. MURPHY, CONCEPTS IN FEDERAL TAXATION G-17 (1995). *See generally* ROBERT SELLERS SMITH, 898 WEST'S TAX LAW DICTIONARY (1993) (defining Technical Advice memorandum).

35. Tech. Adv. Mem. 81-440-06 (July 22, 1981).

36. *Id.*

37. *Id.*

38. *Id.*

education.[39] *Finally, B contended that the gifts of cash to A's two daughters, a daughter-in-law, and his grandchildren to pay life insurance premiums for policies were all part of a comprehensive estate planning program that had been devised and implemented by A and his professional advisors in 1973.*[40]

In ruling whether or not *B* had authority under New York law to make the transfers, the IRS stated that:

> Although no specific language in the . . . Power of Attorney . . . refers to transfers by gift, we rule that the general language of sections 5-1502B, 5-15021I, and 5-1502K of Title 15 of Article 5 of the New York General Obligations Law authorized B to continue the business and personal family affairs of A that A initiated before he executed the power of attorney in favor of B in 1975.[41]

Accordingly, *B* had the authority under New York law to make the transfers of *A*'s property to his family members before *A* died in 1978, and these transfers were not voidable.[42]

In issuing its ruling, the IRS relied specifically on the fact that *A* had a clearly defined estate and gift tax plan that authorized *B* to make the transfers of *A*'s property in writing, even though the power of attorney did not grant this right.[43] Although the Service did not say so, it is clear that it felt comfortable that *B* was acting according to the wishes of *A* and was not exceeding her scope of authority in any way.[44] In fact, the IRS specifically stated that it was not forced to answer the question of whether *B* was authorized to transfer by gift any of *A*'s property that was not related to an annual gift program which was initiated by *A* prior to executing the power of attorney in favor of *B*. This was because *B* had made no such gifts.[45]

In a private letter ruling issued after TAM 81-44-006,[46] the IRS determined that gifts made by an attorney-in-fact who, under Michigan law, had no power to make such gifts on behalf of the principal, would be included in the principal's taxable estate under section 2038 of the Code as a revocable transfer.[47] In so ruling, the IRS noted there was no Michigan authority specifically addressing the issue of

39. *Id.*
40. *Id.*
41. *Id.*
42. *Id.*
43. *Id.*
44. *Id.*
45. *Id.*
46. *See* Priv. Ltr. Rul. 86-35-007 (May 19, 1986).
47. *Id.*

whether an agent under a power of attorney had the authority to make gifts of the principal's property.[48] However, in as much as the instrument gave detailed instructions as to the management of assets but did not contain any specific power to make gifts, the IRS held that such authority could not be considered to have been granted.[49] It was the position of the IRS that the general rule of strictly construing a power of attorney should apply.[50]

Under this rule of strict construction, the instrument will be held to grant only those powers which are specified,[51] and the agent may neither deviate nor go beyond those powers. In other words, the "act done must be legally identical with that authorized to be done."[52] An important corollary to this rule is that where powers are conferred on an agent by a power of attorney, the meaning of general words in the power are restricted by the context. Further, the authority is construed strictly so as to exclude the exercise of any power that is not warranted either by the terms actually used or as a necessary means of executing the authority given.[53] As a result, the IRS interpreted the power of attorney in question not to include gift-giving powers because such authority was not provided for in the instrument.

In Private Letter Ruling 86-23-004, gifts made by an attorney-in-fact under a nondurable power of attorney[54] were included in the gross estate of the decedent/principal pursuant to section 2038.[55] Her agent, acting while the principal was mentally incompetent, made

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48. *Id.*

49. *Id.*

50. *Id.*

51. *See* Lippman v. First Nat'l Bank of Aninston, 24 So. 581 (Ala. 1898); Wysong v. Automobile Underwriters, Inc., 184 N.E. 783 (Ind. 1933); Harris v. Johnston, 55 N.W. 970 (Minn. 1893); Campbell v. Foster Home Ass'n, 30 A. 222 (Pa. 1894).

52. *See* 3 AM. JUR. 3D *Agency* § 31 (1986).

53. *See* Lanaham v. Clark Car Co., 11 F.2d 820, 824 (3d Cir. 1926) ("We construe the general and specific provisions of the power of attorney in the light of the familiar principle of law that general powers in such instruments are limited by the specific powers therein granted." (Woolley, J.)), *remanded*, 31 F.2d 419 (3d Cir.), *cert. denied*, 280 U.S. 559 (1929); RESTATEMENT (SECOND) OF AGENCY § 37 (1958) (The specific authorization of particular acts tends to show that a more general authority is not intended.); *id.* § 65(1) cmt. (a) (When authority is conferred upon an agent by a formal, written instrument, such as a power of attorney, the authority given the agent will be strictly construed so as to exclude any authority not specifically set forth, except authority necessary to effectuate the purpose of the authority granted.).

54. *See supra* note 3.

55. Priv. Ltr. Rul. 86-23-004 (Feb. 18, 1986).

gifts of the principal's property to the principal's grandchildren.[56] The agent filed gift tax returns with respect to the gifts and subsequently excluded these gifts from the decedent's estate when the federal estate tax return was filed.[57]

The Service relied on the applicable local law in interpreting the power of attorney and determined that the agent *could* exercise the power while the principal was incompetent. The actions taken by the agent, however, were voidable by the individual.[58] The Service noted that the durable power of attorney was statutorily recognized by the state and would have granted the attorney-in-fact the power to bind the principal if the principal lacked any disability.[59] All that was needed to satisfy the applicable state statute was evidence of the principal's intent that the power would not terminate upon subsequent disability.[60] Without such intent, as was the case here, any contract or conveyance of property by the agent was voidable by the principal.[61]

The IRS, relying on this distinction under local law, also ruled that the gifts made by the decedent's agent were includable in the decedent's gross estate because section 2038 provides that the gross estate includes the value of property transferred by the decedent over which the decedent holds the power to alter, amend, revoke, or terminate the enjoyment of the beneficial interest on the date of death.[62] Therefore, because the decedent could have revoked the gifts on her date of death, the Service held that section 2038 was applicable to the gifts.[63] According to the IRS then, it is the *potential* rather than the *actuality* of revoking the gift that gives rise to the possibility of including the transferred property.[64]

These two private letter rulings illustrate the hard-line approach the Service has taken against agents making gifts of the principal's assets. In short, the IRS will strictly construe all powers of attorney

56. *Id.*
57. *Id.*
58. *Id.*
59. *Id.*
60. *Id.*
61. *Id.*
62. *Id.*
63. *Id.*
64. The Service relied on the Ninth Circuit decision in Fish v. United States, 432 F.2d 1278 (9th Cir. 1970), and the Third Circuit decision in Pennsylvania Bank & Trust Co. v. United States, 597 F.2d 383 (3d Cir. 1979), which held that a decedent's mental capacity on the date of her death was irrelevant to the legal question of whether she held the right and power to designate who would possess and enjoy the property.

and will hold gifts made under a nondurable power of attorney voidable if the principal was incompetent or incapacitated at the time the gifts were made.

As previously mentioned,[65] an important distinction between a durable and a nondurable power of attorney is that actions taken after a principal's incapacitation will only be binding under a durable power. This distinction was brought to light by the IRS in the previously discussed private letter ruling, and it was interpreted by many estate planners to expressly permit the use of gift-giving powers under a durable power of attorney.[66] In challenging the use of the technique which granted general powers to the attorney under durable powers of attorney, the IRS was victorious in the important decision of *Estate of Casey v. Commissioner*.[67]

In December of 1973, Olive Casey, a resident of Virginia, executed a durable power of attorney appointing her son, Robert, as her attorney-in-fact. The power of attorney was a broad power granting Robert the power to "lease, sell, grant, convey, assign, transfer, mortgage and set over to any person, firm or corporation for any such consideration as he may deem advantageous, any and all of my property."[68] This conferral of specific powers was followed by a general grant of power which authorized Robert to

> do, execute and perform all and every other act or acts, thing or things as fully and to all intents and purposes as I myself might or could do if acting personally, it being my intention by this instrument to give my attorney hereby appointed, full and complete power to handle any of my business or to deal with any and all of my property of every kind and description, real, personal, or mixed, wheresoever located and howsoever held, in his full and absolute discretion.[69]

The granted power contained no specific provision authorizing the attorney to make gifts or to convey property without consideration.

Roughly one year after the power of attorney was granted, the decedent and her husband adopted an estate plan that consisted of making gifts to their sons within the scope of the annual gift tax exclusion.[70] However, the estate tax return filed upon Mrs. Casey's death

65. *See supra* note 3.
66. *See supra* note 46.
67. Estate of Casey v. Commissioner, 984 F.2d 895 (4th Cir. 1991).
68. *Id.* at 896.
69. *Id.* at 897.
70. Typically, the husband would make yearly transfers to the three children and to trusts established for the benefit of their seven grandchildren. The decedent would join in these conveyances made by her husband and consented to treating

did not include the gifts made by her son as attorney-in-fact.[71] The IRS, in reviewing the return, asserted that in the absence of an express grant of authority, a general durable power of attorney did not authorize gifts by an attorney-in-fact.[72] The Service, in accordance with the two private letter rulings discussed above, determined that the gifts were voidable transfers to be included in Mrs. Casey's estate.[73]

The Tax Court ultimately rejected the Service's position and held that the gifts were not includable in the decedent's gross estate.[74] On appeal, however, the Fourth Circuit reversed and held that such transfers by an attorney-in-fact were not authorized under Virginia law and were included in the decedent's estate.[75] The Fourth Circuit, in issuing its ruling, agreed with the Tax Court that the state law governed the voidability of gifts.[76] But whereas the Tax Court found the transfers effective under state law, the appeals court found no support in state law for inferring an unstated power to make gifts in a formally drawn, and otherwise comprehensive, power of attorney.[77] The

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the gifts as being made one-half by her. (Under I.R.C. § 2515(a), if a married person makes a gift to someone other than his spouse, the donor and the donor's spouse may choose to have one-half of the gift to be from each one of them instead of the gift being made entirely by the actual donor. If this "gift-splitting" is elected, the donor can make a gift of up to $20,000 without incurring any gift taxes. *See* STEPHENS ET AL., *supra* note 11, ¶ 10.03). Between 1977 and 1980, the decedent became incompetent to manage her affairs because of Alzheimer's disease, and she remained incompetent until her death in 1989. Consequently, when her husband made additional conveyances to take advantage of his gift tax exclusions in 1980 and 1981, the attorney-in-fact joined in the execution of these transfers to convey the decedent's dower interest in real property. After the decedent's husband's death, the attorney-in-fact continued to make gifts within the ambit of the annual gift tax exclusion pursuant to the power of attorney granted to him. *Estate of Casey*, 984 F.2d at 897.

71. *Id.*

72. *Id.*

73. *Id.*

74. *See* Estate of Casey, 58 T.C.M. (CCH) 176 (1989). The reasons for the tax court's disagreement with the position of the IRS will be examined more closely in the following sections of this note.

75. *See Estate of Casey*, 948 F.2d at 902.

76. The Fourth Circuit was compelled to predict what Virginia's Supreme Court would rule on the issue because of the U.S. Supreme Court's decision in Commissioner v. Estate of Bosch, 387 U.S. 456 (1967). In *Estate of Bosch*, the Court held that where federal estate tax liability turns upon the character of a property interest held and transferred by the decedent under state law, federal authorities are not bound by the determination made of such property interest by a state trial court. *Id.* The Court further held that if there is no decision by the state's highest court, federal authorities must apply what they find to be the state law after giving "proper regard" to relevant rulings of other courts in the state. Consequently, this was what the Fourth Circuit was doing. *Id.*

77. *Estate of Casey*, 948 F.2d at 898.

Fourth Circuit held that if the Virginia Supreme Court ruled on the issue, it might well adopt the flat rule that failure to express this power is to withhold it—because it is an attractive rule if the power is a durable one, and the grantor of the power would be unable to protect himself or herself against abuse.[78] Furthermore, the Fourth Circuit believed that even if the state court chose not to adopt this rule and looked instead to the intent of the decedent at the time she executed the power of attorney, the lower court would still have to conclude that the decedent had not conferred any power to make gifts.[79]

For the Fourth Circuit, the guiding principle in determining whether an attorney-in-fact has certain powers is to examine the principal's intent as manifested in the instrument itself and only look to the surrounding circumstances to clarify ambiguity in the instrument.[80] Based on this approach, the court noted a glaring omission in the instrument—namely the specific power to make gifts or transfers without adequate consideration.[81] According to the court, the power specifically referred to all of the principal methods of asset transfer except for gifts. The court argued that the absence of gift-giving power strongly suggests a specific intent to omit as opposed to an oversight.[82] The court noted that "[w]hen one ponders the care with which this instrument enumerates these specific legal purposes for asset transfer, the omission of gift strongly suggests a positive intent rather than oversight or any opposing intent with respect to that power."[83] In addition, the court concluded that expansive language giving broad authority to the attorney-in-fact should be interpreted as conferring only those incidental powers necessary to accomplish purposes expressly conferred by that authority.[84] Consequently, the

78. *Id.* at 897. The Fourth Circuit believed that the Virginia Supreme Court would apply the general rules of construction when interpreting an instrument such as this and conclude that the gifts made here would be revocable. *See supra* note 14. The court of appeals also thought it possible that Virginia's high court would follow the ruling of the South Carolina Supreme Court in Fender v. Fender, 329 S.E.2d 430, 431 (1985), which held that "in order to avoid fraud and abuse, we adopt a rule barring a gift by an attorney-in-fact to himself or a third party absent clear intent to the contrary in writing." *Id.*

79. *Estate of Casey*, 948 F.2d at 901.

80. *Id.* at 900.

81. *Id.*

82. *Id.*

83. *Id.*

84. *Id.* at 901. The court relied on Hotchkiss v. Middlekauf, 32 S.E. 36, 38 (Va. 1899) (holding that language to the effect of "full power and authority to do and perform all and every act, . . . as fully . . . as I might" should be interpreted as not expanding powers beyond those expressly granted), Brassert v. Clark, 162 F.2d

Fourth Circuit determined that the omission of a specific gift power in the power of attorney was likely to be dispositive to a Virginia court.[85]

The Estate argued that the court should look to extrinsic circumstances, most notably the pattern of gift giving that Mrs. Casey had undertaken, because the gifts issued by the attorney-in-fact simply carried forward the estate plan which Mrs. Casey had joined both before and after execution of the power of attorney. Therefore, the Estate postulated, her pattern of gift giving may imply her intent to authorize its continuation by her attorney-in-fact.[86] The Fourth Circuit reiterated its holding that a court did not need to examine extrinsic circumstances to infer an unexpressed intent to confer a power of gift, but found that even if a Virginia court considered extrinsic circumstances, no such intent could be inferred under this set of facts.[87] The court characterized the pattern of gifts which the decedent had consented to before becoming incompetent as being gifts typically consisting of the husband's property which the decedent had joined for gift tax purposes or for purposes of releasing her dower interest.[88] This "pattern of giving," the court held, was not a pattern of transferring her own assets.[89]

The Fourth Circuit concluded that compelling policy considerations require courts to take care when they are asked to infer powers not expressly authorized by powers of attorney.[90] This is especially the case, the court cautioned, when the power is a "dangerous" one,[91] such as a gift power, and when the power, such as here, is a durable one that survives a principal's personal ability to monitor its exercise.[92]

The Fourth Circuit's decision in *Casey* was a critical one for the IRS because it provided the Service with a definitive judicial ruling on many of the issues that it had confronted in its private letter rulings. Nevertheless, many agents continue to argue that they have authority to make gifts because *Casey* is limited to its facts.

967, 973 (2d Cir. 1947) (to the same effect), and RESTATEMENT (SECOND) OF AGENCY § 37 cmt. a (1958).

85. *Estate of Casey*, 948 F.2d at 901.
86. *Id.*
87. *Id.*
88. *Id.*
89. *Id.* at 902.
90. *Id.*
91. *Id.*
92. *Id.*

For example, in Private Letter Ruling 92-31-003, the Service addressed an agent's transfers of the principal's property pursuant to a durable power of attorney that did not specifically grant gift giving but had been certified by a court order ratifying all of the gifts made under the agency.[93] The IRS ruled that the gifts became complete only on the date of ratification and, as a result, the transfers of property during the years prior to the court order were not completed gifts.[94] Thus, only $10,000 per donee was allowed as an exclusion.[95] The retroactive court order, therefore, was not effective for federal gift tax purposes, and no gift tax exclusion was allowed for all of the gifts that had been made during the other years in question.[96]

In issuing its opinion in Private Letter Ruling 92-31-003, the IRS relied heavily on the *Casey* decision. The Service reiterated the Fourth Circuit's findings and enumerated the four principal ways of transferring assets and noted that the power of attorney included all of them except the power to make gifts.[97]

Although the IRS has issued several Private Letter Rulings dealing with the same issues as in Private Letter Ruling 9231003,[98] this ruling represents the high water mark of the continued attack by the IRS against gifts made by attorneys-in-fact.[99] The IRS made clear in this ruling that unless the power of attorney explicitly states that the agent has the right to make gifts, nothing the attorney-in-fact can do, including judicial ratification, will satisfy the Service that the agent acted with the proper authority.

B. The Response of the Courts

Although a majority of the courts[100] have followed the approach of the Internal Revenue Service in its private letter rulings and the

93. Priv. Ltr. Rul. 92-31-003 (Apr. 9, 1992).
94. *Id.*
95. *Id.*
96. *Id.*
97. *Id.*
98. *See* Priv. Ltr. Rul. 93-47-003 (Aug. 5, 1993); Priv. Ltr. Rul. 94-03-004 (Jan. 21, 1994); Priv. Ltr. Rul. 94-10-028 (Mar. 11, 1994).
99. *Cf.* Estate of Casey v. Commissioner, 948 F.2d 895 (4th Cir. 1991), wherein the attorney had arguably made types of gifts that were materially different from the pattern of gifts made by the decedent prior to the execution of the power of attorney.
100. *See* Zawadski De Bueno v. Bueno Castro, 822 F.2d 416 (3d Cir. 1987); Von Wedel v. McGrath, 180 F.2d 716 (3d Cir. 1950); Aiello v. Clark, 680 P.2d 1162 (Alaska 1984); Fletcher v. Matthew, 448 N.W.2d 576 (Neb. 1989); Fender v. Fender, 329 S.E.2d 430 (S.C. 1985); Wilkinson v. Commissioner, 66 T.C.M. (CCH) 279 (1993).

Fourth Circuit in *Estate of Casey*,[101] not all courts have agreed. In *Estate of Bronston*,[102] a case before the U.S. Tax Court, gifts made by a decedent's son pursuant to a New Jersey power of attorney were not includible in the decedent's gross estate.[103] In this case, the language in the power of attorney conferring authority upon the agent to "grant, bargain, sell, convey, or lease or contract for the sale, conveyance, or lease of any property,"[104] coupled with the personal circumstances of the creation of the power of attorney and the personal conversations of the decedent with her family members, were held to sustain the authority of the agent to make gifts on behalf of the principal.[105]

The Tax Court explicitly rejected the Commissioner's argument that the language in the power of attorney allowed the attorney-in-fact to engage only in business transactions on the decedent's behalf.[106] In applying New Jersey law, the court held that the language authorizing Bronston, "to grant and . . . convey . . . any property now or in the future owned by me . . ." could authorize gifts in appropriate circumstances.[107] The court recognized that, unlike other cases where powers of attorney were not held to include gift-giving authority, such as *Von Wedel v. McGrath*,[108] the decedent's business involvement was minimal and she had no partnership or sole proprietorship interest.[109] Rather, the bulk of her assets were all passive investments managed by an investment company.[110] Furthermore, the court noted that the decedent looked to her son as an attorney-in-fact to provide her with support and medical care as well as to continue her usual practice of giving gifts qualifying for the gift tax exclusion to her family.[111]

Ultimately, the Tax Court found that because the Commissioner could not produce any authority that would suggest "grant and convey" is inappropriate gift language in New Jersey, the words would be given their common-sense interpretations.[112] Therefore, under New Jersey law, Bronston was authorized to make gifts to the dece-

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101. *See supra* note 15.
102. Estate of Bronston, 56 T.C.M. (CCH) 550, 551 (1988).
103. *Id.*
104. *Id.*
105. *Id.*
106. *Id.*
107. *Id.*
108. *Id.* at 552.
109. *Id.* at 553.
110. *Id.*
111. *Id.*
112. *Id.*

dent's family in the same way that such gifts had been made in prior years, i.e., gifts to each child and spouse in an amount that did not require the filing of a gift tax return.[113]

Although the Tax Court in *Estate of Bronston* relied primarily on its interpretation of New Jersey law, it also relied on its earlier decision in *Estate of Gagliardi*.[114] In *Gagliardi*, decided a year before *Bronston*, the Tax Court found that a power of attorney executed in Pennsylvania was broad enough to authorize the making of gifts on behalf of the decedent.[115] In rendering its decision, the court found, as a matter of fact, that the decedent had intended to make the gifts as evidenced by his oral instructions to the attorney-in-fact to take the necessary steps to carry out his intent.[116] Because the decedent's intent was clear, the Tax Court was obliged to follow the Pennsylvania Supreme Court's ruling in *Cost v. Caletri*,[117] which held that when an intent to give a gift is manifested and a power of attorney is "in the circumstances, the most the donor could do to effect delivery,"[118] an effective gift is given by the agent acting under that power.[119]

Both *Gagliardi* and *Bronston* represent the general attitude taken by the Tax Court when faced with the question of whether or not an agent has the authority to make gifts when a power of attorney does not explicitly vest the agent with such power. In fact, only one in-

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113. *Id.*
114. Estate of Gagliardi, 89 T.C. 1207 (1987).
115. *Id.* at 1211. The power of attorney provided that Gagliardi could, among other things,

> execute all instruments and to do all things in all matters, affairs, or properties of any description which I/we may at any time own or be entitled to, to the same extent that I/we could do if present and active, . . . withdraw all or any funds that may be deposited . . . in any bank or trust company, and . . . issue checks or orders against the same, . . . sell, assign, transfer, and deliver all bonds, shares of stocks in corporations, and polices of insurance, . . . and sell and convey all property, real and personal . . . .

Id. at 1208 n.1. It also gave

> [m]y/our said attorney, or his/her substitute or substitutes, full power and authority to do and perform all and every act and thing whatsoever, requisite and necessary to be done in and about the premises, as fully to all intents and purposes as I/we might or could do, if personally present, hereby ratifying and confirming all that my/our said attorney or his substitute or substitutes shall lawfully do or cause to be done by virtue hereof.

Id.
116. *Id.* at 1211.
117. Cost v. Caletri, 394 A.2d 513, 518 (Pa. 1978).
118. *Id.* at 518.
119. 89 T.C. 1207 (1987).

stance has occurred where the Tax Court has ruled in favor of the Internal Revenue Service, and that was a case in which it was clear to the court that the gifts made by the attorney-in-fact were not contemplated by the principal when creating the power.[120]

The Tax Court, however, is not the exclusive judicial body to take aim at the Internal Revenue Service's position regarding gift-giving power and powers of attorney. In 1991, the Supreme Court of Georgia, in *LeCraw v. LeCraw*,[121] held that gifts made by an attorney-in-fact were authorized, even though the power of attorney did not specifically authorize gifts of the principal's property or make any reference to estate planning.

In *LeCraw*, the executors of a decedent's estate in Georgia sought a declaratory judgment regarding the scope of a power of attorney the decedent had granted her three sons.[122] The power did not specifically authorize gift giving, but it did say that they could do " 'any other thing or perform any other act . . . which I might do in person' and stated that 'this shall be a general power of attorney.' "[123] The IRS again asserted that the attorneys-in-fact were not authorized to make gifts and that the gifted property was includible in the decedent's gross estate because the transfers were voidable.[124] The gifts, made during a period of approximately one week, from December 1985 to January 1986, aggregated $650,000.[125]

The court, in issuing its ruling, relied on its earlier decision in *Johnson v. Johnson*.[126] The court recognized that even though a formal power of attorney is subject to a strict construction, and general terms are to be restricted to consistency with the controlling purpose and will not extend authority so as to add new powers, "the agent's au-

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120. *See* Wilkinson v. Commissioner, 66 T.C.M. (CCH) 270, 274 (1993) ("We find it difficult to believe that, as McCulloch's agent, petitioner was authorized to draw checks for the payment of her own credit card bills, medical bills, mortgage, and such.").

121. LeCraw v. LeCraw, 401 S.E.2d 697 (Ga. 1991).

122. *Id.* at 698.

123. *Id.*

124. *Id.* at 698 n.1.

125. *Id.* The gifts were made to approximately 40 persons in the form of checks prepared by a family employee. The checks, drawn on the account of the principal, were each in the amount of $10,000 and included gifts to the attorneys-in-fact individually, to their respective spouses, to their respective children, and to some close family friends.

126. Johnson v. Johnson, 193 S.E. 345 (Ga. 1937).

thority shall be construed to include all necessary and usual means for effectually executing it."[127] The court went on to find that

> [w]here, as here, the grantor of the power of attorney expresses in that document the desires that her business be transacted by her attorneys-in-fact and that the power of attorney be a general power, and the evidence is undisputed that the actions taken by the attorneys-in-fact, unobjected to by the grantor, continue the grantor's practice of giving monetary gifts to the natural objects of her bounty and affection; that the exercise of the power to make gratuitous transfers by the attorneys-in-fact does not deplete the grantor of the assets necessary for her to live her accustomed lifestyle; and that the exercise of the power to make gifts to the natural objects of her bounty minimizes the estate transfer tax, a goal the grantor desired, we construe the general power of attorney executed by the grantor to include within it the power to make gratuitous transfers of property to the natural objects of the grantor's bounty.[128]

The dissenting opinion took the position that a power of attorney should be strictly construed.[129] The dissent relied on the decisions of *Estate of Casey v. Commissioner*[130] and *Fender v. Fender*.[131] The Supreme Court of South Carolina invalidated gifts by a familial attorney-in-fact, in order to avoid potential fraud and abuse in the absence of a clear intent to the contrary.[132]

The Tax Court's decisions in *Estate of Bronston*[133]and *Estate of Gagliardi*,[134] as well as the Georgia Supreme Court's holding in *LeCraw v. LeCraw*,[135] are a minority position. However, these cases, taken in totality, suggest that courts may be more sympathetic to attorneys-in-fact who can demonstrate several critical factors. These factors are: (1) that their actions are pursuant to a general grant of power; (2) that the principal had a history of making gifts for either estate purposes or out of love and affection; and (3) that the gifts do not deplete the principal's assets to the point where the principal can no longer live according to their accustomed lifestyle.[136]

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127. *LeCraw*, 401 S.E.2d at 698.
128. *Id.* at 699.
129. *Id.* at 700-01.
130. *See supra* note 15.
131. *See supra* note 78.
132. *Id.* at 431.
133. *See supra* note 102.
134. *See supra* note 114.
135. *See supra* note 121.
136. Despite this apparent sympathy, as the ruling on appeal by the Fourth Circuit Court of Appeals in *Estate of Casey v. Commissioner* demonstrates, it is possible for an attorney-in-fact to prove each of the listed factors and, nevertheless, lose.

C. Reactions of the States

The decisions cited and discussed above demonstrate the difficulty of determining how a particular court is going to interpret a power of attorney. In fact in one situation, the same court has interpreted two similar instruments in two completely different ways. In *Schmuck v. Dumm*,[137] Judge Wise, for an Ohio court, held that a power of attorney to "do and perform all and every act . . . as I might or could do" did not permit the agent to make gifts. In *Estate of Harold Canaday*,[138] however, the same court reversed and remanded a probate court determination that language in a power of attorney "to act in all matters, legal or otherwise, and to transact business"[139] did not permit the agent to make gifts.[140] In an effort to try to combat the seemingly arbitrary determinations made by the courts, Virginia and Alabama have taken proactive steps which legislate that general powers of attorney executed in their states contain implied authority for attorneys-in-fact to make gifts of the principal's assets.

Virginia amended its power of attorney statute in connection with gift giving in 1992. The amendment provides that a power of attorney which authorizes an agent to do any act that the principal might or could do, or evidences the principal's intent to give the agent power to handle the principal's affairs, impliedly includes the power to make gifts in accordance with the principal's personal history of making or joining lifetime gifts.[141] The Virginia statute also provides that, after reasonable notice to the principal, an attorney-in-fact may petition the court for authority to make gifts of the principal's property consistent with the express terms of the power of attorney. In making its decision on the petition, the court is required to determine the amounts, recipients, and proportions of any gifts taking into account: (1) the size of the principal's estate, (2) the principal's foreseeable obligations and maintenance needs, (3) the principal's personal history of making, or joining in the making of, lifetime gifts, (4) the principal's estate plan, and (5) the tax effects of the gifts.[142]

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137. Schmuck v. Dumm, No. 6133, 1983 WL 6557 (Ohio Ct. App. July 25, 1983).
138. Estate of Harold Canaday, 1988 Ohio App. LEXIS 1396 (Ohio Ct. App. Mar. 7, 1988).
139. *Id.*
140. *Id.*
141. VA. CODE ANN. § 11-9.5 (Michie 1993).
142. *Id.*

The Alabama statute,[143] which became effective May 6, 1994, is similar to the Virginia provision in all respects except its lack of a provision for a petition procedure. The Alabama statute provides that an attorney-in-fact can make gifts only after determining that the gift is either (1) in the principal's best interest, (2) in the best interests of the principal's estate, or (3) that the gift will reduce the estate tax payable on the principal's death and that the gift is in accordance with the principal's personal history of making or joining in the making of lifetime gifts.[144]

Both the Alabama and Virginia statutes explicitly provide that this new legislation does not impair the rights or power of any principal, by express words in the power of attorney or in another writing, to further authorize, expand, or limit the authority of any attorney-in-fact or other agent to make gifts of the principal's property.[145]

D. Judicial Interpretations

In 1993, in *Estate of Ridenour*,[146] the U.S. Tax Court had the opportunity to consider the new Virginia statute. The court held that a Virginia power of attorney, which authorizes the attorney-in-fact to perform acts that the principal might or could do, shall confer authority to make gifts which are in accordance with the principal's personal history of making lifetime gifts, unless expressly provided otherwise.[147]

The facts of *Ridenour* are straightforward. Joseph Ridenour executed a durable power of attorney in 1971 appointing his child, James Ridenour, as his attorney-in-fact.[148] When that power of attorney could not be located, Joseph executed a second durable power of attorney on January 12, 1987, again appointing James as his agent.[149] Joseph became ill in late 1986, and by March 20, 1987, he could no longer effectively communicate with others.[150] On March 27, 1987, James, acting pursuant to the power, made gifts by writing nine checks on Joseph's account in the amount of $9,500 each to himself,

143. ALA. CODE § 26-1-2.1 (Michie Supp. 1994).
144. *Id.*
145. ALA. CODE § 26-1-2.1(b); VA. CODE ANN. § 11-9.5(b).
146. Estate of Ridenour, 65 T.C.M. (CCH) 1850 (1993).
147. *Id.*
148. *Id.* at 1851.
149. *Id.*
150. *Id.* at 1853.

his wife, his four children, and his three grandchildren.[151] Joseph died on April 15, 1987, of kidney failure.[152]

On the federal estate tax return filed for Joseph's estate on January 15, 1988, the $85,500 in gifts were not included in his gross estate.[153] On January 4, 1991, the Commissioner issued a notice of deficiency to the estate based on the Fourth Circuit's decision in *Estate of Casey*.[154] The Estate contested the deficiency by filing a petition with the U.S. Tax Court.[155] While the suit was pending, the Virginia legislature amended its power of attorney statute as discussed above. The Tax Court held that the new statute controlled and that the amount of the gifts was not includable in the gross estate because James Ridenour had implied authority to make the gift irrevocable.[156] The Commissioner appealed the decision of the Tax Court to the Fourth Circuit, asserting that *Casey* was in conflict with the new Virginia statute and that *Casey* should control because the gifts were made closer in time to the date of *Casey*.

The Fourth Circuit specifically rejected the Commissioner's arguments and affirmed the Tax Court's decision that the Virginia statute applied retroactively.[157] In making this finding, the Fourth Circuit recognized that, as a matter of Virginia law, all durable powers of attorney impliedly include authority to make irrevocable gifts during the principal's life so as to be excludable from the principal's federal gross estate.[158] Assuming that the power contains no limiting language, the court apparently will follow the new statute and approve the gifts whenever the general power precedes a list of specific powers and the principal's pattern of giving gifts reveals an intent to take advantage of the tax benefits associated with the distribution of assets.[159]

Although the *Ridenour* decision gave proper effect to the Virginia legislature's amendment, the Fourth Circuit made it clear that its decision was consistent with *Casey*. It was reaffirmed that *Casey* was still good law and to be followed in cases not involving the new Virginia legislation.[160]

151. *Id.*
152. *Id.*
153. *Id.*
154. *See supra* note 67.
155. *Id.*
156. Estate of Ridenour, 65 T.C.M. (CCH) 1850 (1993).
157. Estate of Ridenour v. Commissioner, 36 F.3d 332, 336 (4th Cir. 1994).
158. *Id.* at 334.
159. *Id.* at 336.
160. *Id.* at 334.

Estate of Ridenour is the only case thus far that has interpreted either the Virginia or Alabama provisions. However, it can be plausibly argued that provisions by the state will continue to be upheld and will effectively preclude the IRS from challenging gifts made by attorneys-in-fact if the three conditions emphasized by the Fourth Circuit are satisfied.

IV. Resolution

The power of attorney is a simple yet powerful document which allows an individual full authority to perform almost any act the principal could do personally.[161] As a result of this power, there are "manifold opportunities and temptations for self-dealing."[162] That this is a problem is clear because financial abuse of the elderly is much more widespread than the public generally acknowledges.[163] Although this exploitation occurs in many different ways, such as telemarketing frauds, home repair scams, and thefts of Social Security checks,[164] the worst financial exploitation occurs with durable powers of attorney.[165] In fact, the abuse of powers of attorney has been called an "invisible epidemic," because the victims, who are usually elderly or incapacitated, may be unaware what is happening or too frightened or embarrassed to raise any formal objections which would bring the case to light.[166]

In 1993, the Government Law Center of the Albany Law School conducted a survey which was distributed nationally among attorneys, social service providers, area aging agency administrators, district attorneys, and surrogate court justices. The survey found that ninety-four percent of the respondents believed that durable powers of attorney abuse occurs at least occasionally.[167] Two-thirds of those surveyed reported that they had personal knowledge of abuse, with sixteen percent having encountered it six to ten times, and twenty-two

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161. RESTATEMENT (SECOND) OF AGENCY § 17 (1958).
162. Estate of Casey v. Commissioner, 948 F.2d 895, 898 (4th Cir. 1991).
163. Armond D. Budish, *Giving Power of Attorney a Move Best Made Warily*, THE COLUMBUS DISPATCH, Aug. 19, 1994, at 2D.
164. *Id.*
165. *Id.*
166. Gerald S. Susman, *Power of Attorney Abuse Called Invisible Epidemic*, THE LEGAL INTELLIGENCER, Aug. 20, 1993, at 1.
167. Patricia E. Salkin, *The Durable Power of Attorney: Guarding Against Abuse*, 4 SHEPARD'S ELDER CARE L. NEWSL. (Shepard's/McGraw-Hill, Colorado Springs, Co.), 17, 17 (1994).

percent encountering it ten or more times.[168] The report also found that the abuse is often severe. For example, in forty-eight percent of the cases reported in the study, seventy-five percent or more of the principal's assets were exploited.[169] Finally, the report established that sixty-four percent of the abusers were immediate family members and nineteen were other family members.[170]

As the report confirms, any power of attorney can be the source of abuse. However, the fact that both Virginia and Alabama create a presumption that gifts, even under the most general grants of power to the attorney-in-fact will be valid, suggests that it will be even easier to defraud the elderly in these states. Under these statutes, an attorney-in-fact is given a license to steal from the estate of their principal without any judicial examination and under the guise of the principal's best interest.[171]

In addition to the basic premise that implied gift giving enhances the potential for abuse, most powers of attorney, though simple in nature, are usually drafted with the utmost of care.[172] Keeping this in mind suggests another serious problem with the Virginia and Alabama statutes.

As mentioned previously, there are four principal mechanisms for transferring assets: sale, lease, mortgage, and gift.[173] If a power enumerates these specific legal purposes for asset transfer and omits gift giving as an option, the omission strongly suggests a positive intent not to grant this power, rather than viewing it merely as a drafting oversight.[174] When one contemplates further the feature that distinguishes a gift from all the other purposes, i.e., the lack of value in exchange, a validating reason for the omission is obvious. Unless the power of attorney states otherwise, in a power of attorney which provides that the agent may sell, lease, or mortgage the principal's property, the courts in Alabama and Virginia will now imply the ability to also give the property away, perhaps destroying the intent of the principal.

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168. *Id.*
169. *Id.*
170. *Id.*
171. *See supra* notes 8 and 9.
172. *See generally* Insel, *supra* note 3, at 37.
173. Estate of Casey v. Commissioner, 948 F.2d 895, 900 (4th Cir. 1991).
174. *Id.* In fact, because of the risks and complications associated with gift giving authority, many clients explicitly chose to omit this power. COLLIN ET AL., *supra* note 3, § 4.10, at 4-19.

Finally, implying a gift-giving power in a power of attorney destroys any vestige of a fiduciary relationship between the principal and the agent. As mentioned above,[175] when a power of attorney is executed, a fiduciary relationship between the principal and the attorney-in-fact is created.[176] There are many obligations which arise under such a relationship, not the least of which is the agent's duty to act exclusively in the interest of the principal and forego any personal advantage aside from compensation in the exercise of his or her task.[177] This duty has created the presumption in most states that when an attorney-in-fact makes a gift to him or herself, this gift is presumed to be invalid because it constitutes self-dealing on the part of the agent.[178] Under statutes such as those adopted by Virginia and Alabama, however, no such presumption arises. Instead, it is presumed that the self-dealing gift is valid unless language in the power prohibits the action.

Further supporting this notion that implied gift-giving power destroys fiduciary relations is the fact that making gifts of the principal's estate is never acting exclusively in the interests of the principal. Although many tax advantages can be gained by making such gifts, those advantages are not in the best interests of the principal, but rather in the best interests of his or her heirs! No estate taxes are paid while the principal is alive, and, as a result, it seems tenuous to presume that an agent's giving away of the principal's property ought to be presumed valid.[179]

By suggesting that Virginia and Alabama repeal their legislation, and instead impose a flat rule that gift-giving powers will never be implied in a power of attorney, is not to suggest that attorneys-in-fact should not be given this power. The critical element, however, is that this power should be *given* by specifically enumerating it in the docu-

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175. *See supra* note 3.

176. Although difficult to articulate, a fiduciary is generally one who acts primarily for the benefit of another. *See* HAROLD GILL REUSCHLEIN & WILLIAM A. GREGORY, THE LAW OF AGENCY AND PARTNERSHIP 11 (1990).

177. *Id.*

178. Estate of Casey v. Commissioner, 948 F.2d 895, 900 (4th Cir. 1991).

179. The one instance in which gift giving might be considered in the principal's interests is if he or she has previously engaged in an estate plan which has taken advantage of the gift tax exclusion. However, if this is the case, it seems highly likely that they would include gift-giving authority within the power of attorney so that this practice may be continued. *Cf.* Estate of Ridenour, 36 F.3d 332 (4th Cir. 1994) (despite a history of gifts, the power was not included in the power of attorney); *Estate of Casey*, 948 F.2d 895 (same).

ment.[180] In fact, states, in an effort to combat fraud and abuse, should follow the IRS's lead, and require that all powers of attorney explicitly grant gift-giving powers if a principal wants to vest his or her agent with the power. This per se rule was adopted by South Carolina in *Fender v. Fender*,[181] where the state supreme court held that "in order to avoid fraud and abuse, we adopt a rule barring a gift by an attorney-in-fact to himself or a third party absent clear intent to the contrary evidenced in writing."[182]

V. Conclusion

A power of attorney can be an important, powerful, flexible document, and, when combined with the power to make gifts, can be a useful estate planning tool. However, it can also be a troublesome document that creates the potential for fraud and abuse. Consequently, the principal and the principal's lawyer should consider care-

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180. There are many ways of doing this which will force the Internal Revenue Service to accept the transfer as valid. For example, a clause as simple as: "*Power to make gifts.* My agent is authorized to make gifts, grants or other transfers without consideration, either outright or in trust," would suffice. *See* COLLIN ET AL., *supra* note 3, form 2.91, at F-44. Or the principal could choose to provide a clause as detailed as:

> *Power to make gifts.* I specifically authorize and encourage my-attorney-in-fact to make gifts (outright, in trust, or otherwise) to himself or herself, individually, or to my other children and their descendants, and to the spouses of all my descendants, to the extent such gifts will be eligible for the annual gift tax exclusion provided in Section 2503 (b) of the Internal Revenue Code of 1986, as amended.
>
> However, when a child of mine, his or her spouse, or other descendant of mine is acting as my attorney-in-fact hereunder, gifts to himself or herself in an individual capacity shall be limited to $5,000.00 per year.

Kathleen Ford Bay, *Repercussions of Gifts Under Powers of Attorney—The Ripple Effect*, PROB. & PROP., Nov./Dec. 1989, at 6.

These two examples suggest that several important considerations should go into deciding whether or not to include such a power. Questions such as whether the gift-giving power should be restricted to a limited group of recipients (e.g., the principal's children) in limited amounts (e.g., no more than the federal gift tax annual exclusion amount), or, if a child should be the agent, whether they should have the power to favor themselves over other children, and whether there is a risk that the gift-giving power will be used to distort the principal's estate plan, should all be addressed as well as the possible inadvertent creation of a power of appointment in the attorney-in-fact which may frustrate the tax planning of the attorney-in-fact. *See generally* Insel, *supra* note 3, at 37; Sanford J. Schelsinger & Barbara J. Scheiner, *Estate Planning Using Power of Attorney*, TR. & EST., July 1992, at 38.

181. Fender v. Fender, 329 S.E.2d 430, 431 (S.C. 1985).

182. *Id.*

fully whether to include the gift-giving power among those powers given to the attorney-in-fact. In this vein, Virginia and Alabama should repeal their power of attorney statutes which imply gift-giving powers. By implying such a power, these statutes only exacerbate the potential for abuse and fraud. Instead, all states should adopt a prophylactic rule barring agents from making gifts for any purposes, including taking advantage of the annual $10,000 gift tax exclusions, without explicit authority provided in the power of attorney.