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Gifts with Powers of Attorney

Are We Giving the Public What It Wants?

By Kate Mewhinney

The word “gift” conjures up a surprise in wrapping paper and ribbon. Unfortunately, when it comes to giving gifts under a power of attorney, often the unhappy surprise is that the gift that is needed cannot be given.

Gift-giving by agents under a power of attorney is important in the context of the federal/state program known as Medicaid,¹ which pays for half of all nursing home care.

Gifts or transfers by older citizens can only be made by competent persons or their properly authorized agents. In addition to “Medicaid planning” to preserve their assets, nursing home residents are legally permitted to provide for certain people, such as a spouse or disabled child.

Powers of attorney often fail for one of two reasons. The person signed a statuto-

ry “short form” power of attorney with limited or no authority to make gifts. Or the person used an attorney-drafted document that negates the utility of the gift power. Too many attorneys include gift-provisions that are suitable for the Mercedes owner, when the client is still paying off a Chevy. In either case, the problem is only discovered when the principal is no longer competent—and thus unable to cure the problem by executing a new document.²

The first problem can be resolved by an amendment to statutes like the North Carolina statutory power of attorney that would broaden the powers in the widely used form. The second is not so easily solved, but the beginning point is increasing the knowledge of lawyers who draft powers of attorney so that they

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Editor's Note
See endnote 1 for recent federal law.

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appreciate the importance of giving under government benefit programs.

The problem typically arises when the client goes to a lawyer for a will, and learns about the benefits of a power of attorney for possible incapacity. This is most obviously useful for the older client likely to become reliant on relatives. The power of attorney allows another person, the agent or attorney-in-fact, to make financial decisions for the client, the principal. The agent is a fiduciary and can only act for the principal's benefit.

Giving away the principal's property, especially to the agent himself, is a breach of fiduciary duty unless specifically authorized. In most states, the principal may allow gift-giving by simply adding that power. Such "gifting" powers have long been standard elements in the documents drafted for the well-to-do to enable them to preserve wealth for the next generation by avoiding federal estate tax. But the gift-giving powers used by the wealthy—under the "Mercedes" version of a power of attorney—are often inappropriate for lower- and middle-class clients.

Moreover, transferring real estate by a power of attorney lacking appropriate authority can be a trap. The transferee does not get a good title, so the buyer cannot get title insurance. Like the inadequate power of attorney itself, the problem becomes apparent when it is far too late to cure. North Carolina's elder law practitioners are beginning to study how the short form could be amended to offer gifting options that better fit the financial demands that families encounter. Also, we are getting the word out to practitioners that the gifting power drafted for the wealthy client might not accomplish the goals of their other estate planning clients.

**The Short Form Power of Attorney—
Short but Not Sweet**

North Carolina is one of 17 states that provide for an optional statutory power of attorney, known as "the short form." The short form's extremely limited gift authority often precludes families from preserving property when the principal needs nursing home care.

Who uses it? Often, it is the attorney who does not do high-end estate planning. Or the form is used without a

lawyer and is obtained from the Internet or computer software.

The person executing the North Carolina statutory short form power of attorney indicates, by initialing options, which powers she wants to give the agent.³ These can include real estate transactions, banking, and other familiar categories.

The gifting options in the short form permit:

- (14) Gifts to charities, and to individuals other than the attorney-in-fact
- (15) Gifts to the named attorney-in-fact

Putting aside whether nonlawyers understand "gifts to the named attorney-in-fact," they surely do not realize that the power is limited by statute to gifts "... in accordance with the principal's personal history of making or joining in the making of lifetime gifts."⁴ It is hard to imagine a client who has a history of giving away his or her home or an interest in the home, or other significant assets. But such gifts are exactly the option that competent people often select when faced with the enormous costs of nursing home care. For the client who has lost competence, though, it is too late to execute a new power of attorney.

For many clients, the attorney's failure to offer a broader "gifting power" may be costly. One option is this provision: "I authorize my agent to transfer my property for the purpose of qualifying me for governmental medical assistance." The provision can be enhanced by specifying to whom property transfers can be made and in what shares.

**Nursing Home Care . . . or "What the Client
Least Wants to Talk About"**

Nursing homes and assisted living arrangements are an unappealing topic. But given the odds of needing care and the limited resources of most people to pay, clients executing powers of attorney should consider how they want the agent to proceed if nursing home care becomes necessary. The client might well direct that all of her resources be used to pay for her care, until depleted. No gift power would be needed. But for the client who prefers to pass something to her family, an appropriate gift power is necessary if the power of attorney comes into play.

What are the odds? Most people over 60 will need long-term care for some time.

Medicare, contrary to widespread belief, covers very little nursing home care. About half the cost of care is paid by private payment (savings or insurance) and about half by Medicaid. Two out of three people who enter nursing homes as private pay residents exhaust their resources within one year and then rely on Medicaid.

Three aspects of Medicaid must be addressed if people are to make an informed choice about allowing gifts to be made with their powers of attorney: strict asset limits, estate recovery, and approval of some asset transfers. The person who obtains the statutory short form needs a form that includes an option for gifts and that still achieves eligibility for governmental assistance.

First, the asset limits. Consider the widow who has a home, \$50,000 in savings and \$1,000 per month income. Medicaid asset limits mandate that all but \$2,000 of the savings must be spent before Medicaid will begin to pay. In most cases, she is allowed to keep the home. This client should be asked whether she wants to allow her agent to take some of the excess savings out of her bank account, to bring her down to the Medicaid asset limit.

Second, what must one know about Medicaid's claims against a person's estate, or "estate recovery"? Unlike Medicare or any health insurance you are familiar with, the Medicaid nursing home program essentially runs a tab on each recipient. With few exceptions, the state demands to be repaid. After a year on Medicaid, in our example the estate recovery claim would be about \$42,000 and after two years \$84,000. Soon there is no house or other asset left in the estate. This part of the equation can make the most artfully drafted will merely a futile gesture. Within the strictures of increasingly difficult Medicaid asset transfer rules, however, the client may want to avoid estate recovery by taking the home or other assets out of his or her name.

Third, federal Medicaid law *allows* families to protect some assets by transferring them.⁴² U.S.C. § 1396p(c)(2)(B). In particular, it permits transfers to a spouse or a disabled child. A home may

be transferred to a caregiver adult child or a sibling co-owner. Any asset may be transferred to a trust for the sole benefit of any disabled person under age 65.

Without a gifting power, taking assets would amount to a breach of fiduciary duty, and perhaps a crime or at least a violation of state laws barring financial abuse of the elderly. Also, if the transferred asset is real property, it would be impossible for the transferee to later sell the property if a potential buyer tried to get title insurance. Why? The title insurance company would, most likely, check to see if this seller had good title, and without a gifting power held by the transferor, the gift deed would not have transferred good title.

An important and common reason to include a gifting power is to provide for one's spouse. To protect the healthy spouse from impoverishment, federal law permits a "resource allowance." If the couple's assets are in the name of the incapacitated spouse, the "resource allowance" must be retitled to the healthy spouse. This can best be accomplished using a power of attorney with a gift power.

Without a broad gifting power, the family can seek guardianship. Court supervision and permission for asset transfers will probably be required. Another option, not limited to married couples, is a special proceeding for approval to add a gift power. Both of these procedures cost money and take time. It is a lot to ask of families who are already under tremendous stress.

Gift and Estate Tax Considerations Are Only One Factor

The second problem with the gift powers found in many powers of attorney is that they are written for the Mercedes owner when the client drives a Chevy. Federal estate and gift tax considerations should not dictate the scope of a gifting provision for such clients. In any event, they need to be balanced against the issue of Medicaid.

Many powers of attorney limit the agent to making annual tax exclusion gifts. These are gifts to individuals up to \$12,000 per person per year, which are excluded from the federal gift tax. This amount is not sufficient to fund the "resource allowance" for a spouse or to

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transfer a home to a disabled child.

Second, some attorneys are concerned that overly broad gifting powers will expose clients to federal estate taxes by creating a general power of appointment.⁵ This would cause the principal's estate to be included in the agent's taxable estate if he predeceases the principal.⁶ The problem, not widespread, is avoided by requiring written concurrence for gifts to be given by someone other than the agent, typically one of the principal's other adult children or by a "special agent."

Ethical and Policy Issues Large and Small

Gifting powers raise big issues—from the microclimate of the attorney-client relationship on up to the level of distributive justice and social needs.

For practitioners, our goal is to provide an atmosphere that allows the client to make free choices regarding the gifting power. We ask whether the older person is being pressured to protect assets for his or her family. Careful practitioners assess the family dynamics, meeting privately with the older client to elicit her goals.⁷ Some attorneys will not accept payment of fees from the client's adult children, although the ethical rules allow this. Procuring the document or taking the lead in client meetings to control the client is indicia of undue influence.

A broad gifting power may open the door to exploitation, especially of marginally competent older clients.⁸ Mandatory disclosure language on the form would address this to some extent. Also, if the gift language is free of jargon, people will better understand the import of the power being granted.

Another concern for the practitioner is that a broad gift power allows an agent to frustrate the principal's testamentary goals by divesting assets differently. There are solutions. One is to draft the gift provision to require gifts in accordance with the principal's will or with intestacy laws. Another is to require consent of all adult children to major gifts.

Some will oppose broader gifting options because they feel that Medicaid planning itself is against sound public policy, whether by a competent person or by his agent. They make two arguments.

First, they argue that assisting clients to

needlessly become Medicaid eligible is unethical. A program intended for the poor, they contend, is being manipulated so that the middle class can shift their responsibilities to the public. Elder law attorneys would respond that we have the duty to present legal options. Certainly tax lawyers would not withhold advice from their clients to keep the federal deficit from growing. In any event, most attorneys find that they are assisting families with modest means to avoid the rapid impoverishment that results from a \$60,000 annual nursing home bill.⁹

A similar argument is that gifting in powers of attorney to obtain governmental benefits undercuts personal responsibility and planning. Of course, that is true of all insurance, private as well as public. But most long-term care is being provided free by family members, strong evidence that personal responsibility and ethics are alive and well. And an increasing number of people are planning ahead by purchasing long-term care insurance, though it is too expensive for many people.¹⁰ While a comprehensive discussion with the client should include mention of the insurance option, this product is extremely difficult to assess. Moreover, those with chronic health problems are told that they need not apply.

Rather than question the ethics of Medicaid estate planning, perhaps we should ask whether our country's health care system itself is ethical or even logical.¹¹ Medicare covers expensive surgery, but not the devastating costs of chronic illnesses and strokes.

Are these priorities in line with our moral values? Should we be looking at ways to ethically spread the tremendous burdens of caring for the disabled elderly? The desire to leave a legacy to one's children and grandchildren is a universal desire, not limited to the wealthy.

Proposed Changes

Statutes like the North Carolina short form power of attorney are overdue for changes to better serve the public's needs. An option for gifts to obtain governmental assistance should be considered. And the estate and gift tax restrictions that apply to the few should not be thoughtlessly included as the only

standard for making gifts in the powers of attorney of the vast majority of people. These changes would be two welcome gifts for the public. ■

Endnotes

1. Important Update: The Deficit Reduction Act of 2005 (DRA), signed by President Bush on February 8, 2006, made significant changes in Medicaid rules. The changes most relevant to this article limit individuals' ability to transfer assets in anticipation of expensive nursing home care. For example, the "lookback period" for most transfers used to be 36 months; it is now 60 months. And, the period of the disqualification will start when the applicant is otherwise Medicaid eligible, instead of starting when the transfer is made. Some types of asset transfers, however, are still permitted, without causing a period of Medicaid ineligibility ("transfer sanction") or disqualification. Practitioners will need to monitor developments in their state, as the DRA is implemented. The overall point of this article, however, remains valid and that is that statutory "short form powers of attorney" and "annual exclusion amount gifting" provisions are inappropriate for most clients. For an excellent overview of the DRA changes, and the statutory cites, see the website of attorney Tim Takacs, at <http://www.tn-elderlaw.com/060208-dra1396p-1396r-5.pdf>.

2. The author thanks Karen W. Neely for research when she was a student in The Elder Law Clinic, and elder law attorney Ron M. Landsman, of Rockville, Maryland, for critiquing a first draft.

3. A colleague describes seeing an attorney-prepared short form on which not a single power had been initialed, so the document accomplished nothing for the client!

4. N.C.G.S. § 32A-2(15).

5. IRC § 2041.

6. In many elder law cases, gift and estate taxation will not be relevant since the assets of both the principal and the agent are less than the exemption equivalent of the unified credit. Andrew H. Hook, "Durable Powers of Attorney: They are Not Forms!" National Academy of Elder Law Attorneys' Symposium 2000, pp. 1-51, 13.

However, some argue that an unlimited gifting power does not risk creating a general power of appointment because the creator of the power must join in making the gift, at least by failing to revoke the power. See V. Tate Davis, "Basics of Elder Law," *Potpourri for the GP (NCBF CLE)*, 4/29/05, fn. 50.

7. An North Carolina State Bar ethics opinion provides that lawyers may not prepare a power of attorney for the benefit of the principal at the request of another individual or third-party payer without consulting with, exercising independent professional judgment on behalf of, and obtaining consent from the

principal. 2003 FEO-7. Another tool for attorneys is a recent ABA brochure, "Understanding the Four C's of Elder Law Ethics." www.abanet.org/aging/lawyerrelationship.pdf

8. Timothy Takacs and David McGuffey, *Revisiting the Ethics of Medicaid Planning*, NAELA QUARTERLY, Summer 2004, pp. 29-37, 33.

9. Ellen O'Brien, "Issue Brief: Medicaid's coverage of nursing home costs: Asset shelter for the wealthy or essential safety net?" Georgetown University Health Policy Institute, Long-Term Care Financing Project, May 2005; "Long-Term Care Financing: Growing Demand and Cost of Services Are Straining Federal and State Budgets," U.S. GAO, 4/27/05, GAO-05-0564T, p. 7. Charles P. Sabatino, *Debunking the Myths of Medicaid*, LEGAL TIMES, 1/26/04, p. 25; "Private Long-Term Care Insurance: A Viable Option for Low and Middle-Income Seniors?" Kaiser Commission on Medicaid and the Uninsured (15 Feb. 2006) www.kff.org/uninsured/upload/7459.pdf.

10. Fifteen percent or less of middle-aged or elderly persons in North Carolina might conceivably purchase long-term care insurance, based on wealth and income levels necessary to afford such a policy. Donald H. Taylor Jr., Ph.D.; *Alzheimer's Disease and the Family Caregiver: The Cost and Who Pays?* NC MED J., Jan./Feb. 2005, Vol. 66, No. 1, 18-24, 24.

11. Germany and Japan have universal long-term care insurance. "International Approaches to Long-Term Care Financing and Delivery," Global Report on Aging (AARP), Winter 2004, p. 5.

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