

Which Powers of Appointment Are Eligible for a Step-up in Basis in 2010 under the Modified Carryover Basis Rules?

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If you look at Internal Revenue Code Section 1022 too quickly, you may conclude that a decedent's estate in 2010 cannot ever receive any step-up in basis by virtue of any power of appointment. After all, Section 1022(d)(1)(B)(iii) specifically states: "The decedent shall not be treated as owning any property by reason of holding a power of appointment with respect to such property." A deeper look into Section 1022, however, can reveal step-up opportunities.

Perhaps what Congress was trying to do with 1022(d)(1)(B)(iii) was eliminate certain tax games with powers of appointment. One such game was to grant a general power of appointment to a spouse to attempt to receive a complete step-up in basis on the assets affected by it. By making the surviving spouse's trust property subject to a limited, general power of appointment for debt payment during administration of the deceased spouse's estate, the surviving spouse's appreciated trust property would be included in the gross estate of the first spouse to die. Section 1022(d)(1)(B)(iii) would kill this abusive tax game.

Under Section 1022(e)(2)(A), the step-up in basis is available in 2010 to a trust "with respect to which the decedent reserved the right to make any change in the enjoyment thereof through the exercise of a power to alter, amend or terminate the trust." That language, in part, describes a power of appointment that is reserved (as opposed to one that is granted to another person). Thus, a trust with a reserved power of appointment seems to be deemed "acquired" from the decedent under Section 1022(e). The problem is that to qualify for the step-up in basis under 2010 tax law, an asset must also be considered to be owned by the decedent under Section 1022(d), and powers of appointment are generally excluded, but if Congress didn't already believe that a decedent with a reserved power of appointment over a trust owned the trust's assets at the time of death for purposes of Section 1022(d), then why would Congress have included Section 1022(e)(2)(A)? Congress is deemed to know that a reserved power of appointment causes the powerholder to be treated during lifetime as the owner of the trust for income tax and capital gains tax purposes under the grantor trust rules in Sections 671-679. I conclude that a reserved power of appointment in a trust allows the opportunity for a step-up in basis.

What about a reserved power of appointment in a deed? Back in 1990-1992, when the field of elder law was young, I proposed in several articles (including in [Estate Planning](#), [NAELA Quarterly](#) and [The ElderLaw Report](#)) that a power of appointment could be reserved in a deed to avoid treatment as a completed gift and cause a step-up in basis. Many of such deeds may now be in existence. Where the gift was incomplete when the deed was recorded, and is not completed until the powerholder's death, the property is still owned by the decedent for estate and gift tax purposes at the time of death, and passes without consideration at that time, so such a deed may be eligible for the step-up in basis. Still, due to the literal language in Section 1022(d)(1)(B)(iii), it may be considered a stretch to obtain the step-up in basis in 2010, but if all of the parties involved in the deed were to transfer their interests to an irrevocable trust that mirrors the terms in the deed, the step-up possibility would be strengthened. If the holder of the

reserved power of appointment in the deed also reserved a life estate, however, the step-up could be obtained via the reserved life estate. See [Why DOESN'T a Reserved Life Estate Get a Step-up in Basis under Internal Revenue Code Section 1022?](#) and [More about Whether Life Estates Are Eligible for a Step-up in Basis in 2010](#)