UT LAW CLE THE UNIVERSITY OF TEXAS SCHOOL OF LAW

PRESENTED AT

2024 Stanley M. Johanson Estate Planning Workshop

December 6, 2024
Austin, Texas

ESTATE PLANNING FOR MODEST ESTATES:

PRACTICAL TOOLS EVERY PLANNER SHOULD KNOW

Mickey R. Davis
Melissa J. Willms

Mickey R. Davis
Melissa J. Willms
Davis & Willms, PLLC
Houston, TX

mickey@daviswillms.com
melissa@daviswillms.com
281.786.4500

ESTATE PLANNING FOR MODEST ESTATES:
PRACTICAL TOOLS EVERY PLANNER SHOULD KNOW

By

Mickey R. Davis and Melissa J. Willms
Davis & Willms, PLLC
Houston, TX

I. Introduction 1
II. Federal Estate, Gift, and GST Tax Laws 1
A. Permanent, Unified Transfer Tax System 1
1. Historical Perspective 1
2. American Taxpayer Relief Act of 2012, P.L. 112-240 1
3. Permanency 2
4. Portability 2
5. Tax Cut and Jobs Act of 2017, P.L. 115-97 2
6. The Net Investment Income Tax 3
III. Tools Every Estate Planner Should Know How to Use 3
A. Fundamental Tools 3
1. Wills and Revocable Trusts 4
2. Durable Power of Attorney 5
3. Medical Power of Attorney 6
4. Directive to Physicians 6
5. Physician Orders for Life-Sustaining Treatment ("POLST") 6
6. Authorization for Disclosure of Protected Medical Information 7
7. Declaration of Guardian for Children 7
8. Declaration of Guardian for Oneself 7
9. Appointment of Agent for Disposition of Remains 8
10. Organ and/or Body Donation. 8
11. Coordinating Non-Probate Assets. 8
B. Outright Gifting 9
1. What to Give 10
2. Clawback 10
3. Gift Tax and the Three-Year Rule 12
4. Carryover Basis 13
5. Disclosure to the Client 13
6. Income Tax Issues 13
7. Giving Discounted Assets. 13
8. Gifts By Both Spouses. 14
9. End-of-Life or End-of-Year Gifts 14
10. Qualified Tuition and Qualified Medical Payments 15
C. Intra-Family Loans 15
1. Section 7872 Loans 16
2. Term Loans 16
3. Demand Loans 16
4. Note Terms 16
5. Impact of Interest Rates 17
6. Income Tax Issues 17
7. Death During Term 17
8. Use with Grantor Trusts. 17
9. Rates and Yield Curves 18
10. Current Rates 18

11. Using a Balloon Note. 18
12. Payment at Maturity 18
D. Irrevocable Life Insurance Trusts 19
1. Structure 19
2. Incidents of Ownership 20
3. The Three-Year Rule 20
4. The Life Insurance Trust as a Grantor Trust 20
5. Split-Dollar Arrangements. 21
E. Spousal Lifetime Access Trusts 21
1. Structure of the SLAT 22
2. Giving Property to the Trust 22
3. Grantor Trust Implications 23
4. What Benefits Can the Grantor Retain? 23
5. What if the Spouses Divorce? 24
6. Benefit to Heirs 24
7. GST Tax Issues 24
8. Non-Reciprocal SLATs 25
9. SLAT Strategies. 25
F. Grantor Retained Annuity Trusts 26
1. Structure 27
2. Setting the Annuity 27
3. Gift on Formation 27
4. Impact of Interest Rates 27
5. Zeroed-Out GRATs 28
6. Multiple GRATs 28
7. Grantor Trust Implications 28
8. Death During GRAT Term 28
9. Payments in Kind 29
10. Benefit to Heirs 29
11. GST Tax Issues 29
12. Short-term vs. Long-term GRATs 30
13. Insuring the GRAT 30
14. Other Limitations of GRATs 30
G. Qualified Personal Residence Trusts 31
1. Structure. 31
2. Residence, Cash, and Proceeds 32
3. Gift Tax Considerations 32
4. Estate Tax Considerations 32
5. Income Tax Considerations 33
6. Joint Purchase of Residence 33
H. Sale to an Intentionally Defective Grantor Trust 34
1. Structure of the IDGT 35
2. Seeding of Trust. 35
3. Impact of Interest Rates 35
4. Servicing the Debt 36
5. Grantor Trust Implications 36
6. Death of Note Holder 36
7. Benefit to Heirs 37
8. GST Tax Issues 37
9. Selling Discounted or Hard to Value Assets 37
10. Lack of Certainty and Planning Cautions 39
I. Accidentally Perfect Grantor Trusts 40
1. Structure of the APGT 41
2. Basis Issues 42

3. Impact of Interest Rates 42
4. Benefit to Heirs 43
5. Income Tax Issues 43
6. Estate Tax Issues. 43
7. GST Tax Issues 44
8. Selling Discounted Assets 44
9. Combining with Other Techniques 44
IV. Charitable Planning 44
A. Cash Gifts 45
B. Gifts of Appreciated Property 45
1. Gifts to Public Charities. 45
2. Gift to Private Foundations. 46
3. Gain on Sale and Assignment of Income 46
C. Gifts of Qualified Appreciated Stocks 46
D. Tax-Free IRA Distributions 46
1. Structure. 47
2. Income Tax Considerations 48
E. Qualified Charitable Distributions to Split-Interest Entities 49
F. Donor Advised Funds 50
1. Structure. 50
2. Gift Tax Considerations. 51
3. Estate Tax Considerations 51
4. Income Tax Considerations 51
5. Excise Tax Considerations 51
V. Planning Considerations for Transfers at Death 52
A. Portability 52
1. New Vocabulary 53
2. Overview of Regulatory Provisions and Observations about Portability 53
3. Portability vs. Bypass Trusts 63
4. Use with Bypass Trusts - It's Not "Either/Or" 64
5. Estate Administration Musts 64
B. Advantages of Trusts over Outright Bequests 65
1. Control of Assets 65
2. Creditor Protection 65
3. Divorce Protection 65
4. Protection of Governmental Benefits 65
5. Protection from State Inheritance Taxes. 66
6. Income Shifting 66
7. Shifting Wealth to Other Family Members 66
8. No Inflation Adjustment for DSUE Amount 66
9. Risk of Loss of DSUE Amount 67
10. No DSUE Amount for GST Tax Purposes 67
11. Must File Estate Tax Return for Portability 67
12. Impact on Life Insurance Planning 67
C. Using Bypass Trusts 68
1. No Basis Adjustment at Second Death 68
2. Higher Ongoing Income Tax Rates 68
3. Some Assets Cause Greater Tax Burdens 69
4. Disclaimer Bypass Trusts 69
D. Using QTIPable Trusts 70
1. Control, Creditor, and Divorce Protections 70
2. Less Income Tax Exposure 70
3. New Cost Basis at Second Spouse's Death 70
4. Preservation of GST Tax Exemption 70

5. QTIPs and Portability 71
6. QTIPs and Using the DSUE Amount 71
7. No "Sprinkle" Power 72
8. Estate Tax Exposure 72
9. Income Tax Exposure 73
10. Is a QTIP Election Available? 73
11. *Clayton* QTIP Trusts 73
12. The QTIP Tax Apportionment Trap. 74
E. Is a Life Estate Power-of-Appointment ("LEPA") Trust a Better Choice? 75
1. Structure of LEPA Trusts 75
2. Benefits of LEPA Trusts 75
3. Disadvantages of LEPA Trusts 75
VI. Conclusion 76

EXHIBIT A: Historical Estate & Gift Tax Exclusion and GST Tax Exemption Amounts & Top Tax Rates (1916-2025) 77
EXHIBIT B: Sample Pre- and Post- Nuptial Clauses Regarding Portability 78
EXHIBIT C: Sample Letter Regarding Portability 80
EXHIBIT D: Sample *Clayton* QTIP Trust Language 81
EXHIBIT E: Technique Comparison 82

APPENDIX: Overview of Charitable Deduction Rules 83

ESTATE PLANNING FOR MODEST ESTATES: PRACTICAL TOOLS EVERY PLANNER SHOULD KNOW[1]

By

Mickey R. Davis and Melissa J. Willms
Davis & Willms, PLLC
Houston, TX

I. INTRODUCTION

Estate planners have traditionally focused not only on planning for wealth transfers, but also on minimizing taxes associated with the transfer of a client's assets. Legislation that has dramatically increased the federal gift and estate tax exclusions over the past decade has changed the estate planning landscape for all but the wealthiest clients. Even with the scheduled halving of those exclusions in 2026, the availability of the portability of exclusions between spouses at death means that estate taxes are of no concern to many clients. All of this doesn't mean that we have had to throw out the estate planning toolbox and start over; it just means we have had to look at our tools with fresh eyes. In doing so, we find that, with a little polish, our existing tools can help our clients in new ways.

II. FEDERAL ESTATE, GIFT, AND GST TAX LAWS

A. Permanent, Unified Transfer Tax System

1. Historical Perspective

Prior to 2002, each person had a "unified" transfer tax credit which could be used to offset estate and gift taxes. IRC §§ 2010, 2505. This credit effectively sheltered a set amount of transfers (by gift or at death) without incurring any transfer tax. The Economic Growth and Taxpayer Relief Reconciliation Act of 2001, P.L. 107-16, 115 Stat. 38 (2001) ("EGTRRA") "de-unified" the estate and gift tax credit, with the estate tax exemption exceeding the $1 million lifetime gift tax exemption from 2004 through 2009. The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, P.L. 111-312, 124 Stat. 3296 (2010) ("TRA 2010") reunified the estate and gift tax exclusions and the GST tax exemption, increasing them to $5 million for 2011, with an inflation adjustment in 2012. In 2013, the law was scheduled to revert to the law in effect in 2001, immediately prior to the enactment of EGTRRA.

2. American Taxpayer Relief Act of 2012, P.L. 112-240

The American Taxpayer Relief Act of 2012, P.L. 112-240, 126 Stat. 2313 (2013) ("ATRA") was passed by Congress on January 2, 2013 and signed into law on January 4, 2013. ATRA adjusted tax rates and made the changes to the gift and estate tax exclusions and the GST tax exemptions first enacted in 2010 "permanent," while increasing the effective federal estate tax rate on the excess from 35% to 40%. As a result, ATRA kept the estate, gift, and GST tax laws unified with an exclusion of $5,000,000, adjusted annually for inflation after 2011, and a top estate, gift, and GST tax bracket of 40%.[2] For 2017, after applying the inflation adjustment, this exclusion was $5,490,000. For reference, a chart outlining the estate, gift, and GST tax exemptions since 1916 is attached as Exhibit A. At the same time, federal income tax rates were increased for individuals, trusts, and estates to 39.6% for ordinary income and to 20% for qualified dividends and capital gain tax.

---

[1] Some of the material in this paper was submitted as part of the paper presented by Turney P. Berry, Robert K. Kirkland, Suzanne Brown Walsh & Melissa J. Willms, *Not Too Rich, Not Too Poor: Goldilocks Planning for the Middle-Rich Clients Who Need Our Help*, 57th ANN. HECKERLING INST. ON EST. PL. (2023).

[2] Of course, a client may make lifetime use of his or her GST tax exemption without making a corresponding taxable gift, or may make a taxable gift without allocating GST tax exemption. As a result, at death, the remaining amount of these exemptions may be unequal or out of sync.

3. Permanency

As we all know, tax laws are never truly permanent. However, for the first time since 2001, ATRA meant there was no set expiration date for the estate, gift, and GST tax laws. From 2001 to 2013, the estate tax rules had expiration dates with a possibility that Congress would make them "permanent." There was continued uncertainty about "will they or won't they," but with ATRA's unexpiring exclusions, it literally meant that it would take an act of Congress to make a change. And then came December 2017.

4. Portability

TRA 2010 added, and ATRA made permanent, the notion of "portability" of a deceased spouse's unused exclusion amount. In essence, portability provides that upon the death of one spouse,[3] the executor of that spouse's estate may file an estate tax return and elect on that return to allow the surviving spouse to effectively inherit any unused federal estate tax exclusion of the deceased spouse. In other words, the deceased spouse's unused exclusion amount can be "ported" to the surviving spouse. IRC § 2010(c)(2)(B). Final regulations were issued effective June 12, 2015 which provide guidance regarding portability. Treas. Reg. §§ 20.2010-2, -3. The unused exclusion amount is referred to in the statute as the "deceased spousal unused exclusion amount," otherwise known as the "DSUE amount." Once a spouse receives a DSUE amount, the surviving spouse can use the DSUE amount either for gifts by the spouse or for estate tax purposes at the surviving spouse's subsequent death. An individual can only use the DSUE amount from his or her "last deceased spouse." TCJA did not change the rules for portability. As a result, married couples can effectively shelter up to $27.22 million (using 2024 figures) in wealth from federal gift or estate tax without utilizing any sophisticated estate planning techniques.

5. Tax Cut and Jobs Act of 2017, P.L. 115-97

With the passage of TCJA 2017, we lost permanency. TCJA 2017 essentially doubled the estate and gift tax exclusions and GST tax exemption for persons dying and transfers made between 2018 and 2025. As a result, we have unified estate, gift, and GST tax laws with an exclusion (and GST tax exemption) temporarily set at $10,000,000, adjusted annually for inflation after 2011[4] (scheduled to return to $5,000,000 after 2025, but adjusted for inflation after 2011), and a top transfer tax bracket of 40%. For 2024, after applying the inflation adjustment, the exclusions and exemption are $13,610,000.[5] TCJA 2017 also adjusted income taxes, lowering the top bracket to 37% for ordinary income. Changes to the income tax rates maintain a spread between the top tax

---

[3] A "spouse" may include persons other than those ceremonially married in the jurisdiction in which the decedent died. For example, persons who are married under the common law of one jurisdiction may be recognized as married for federal tax purposes, even if they later move to a jurisdiction that does not recognize common law marriage. *See* Rev. Rul. 58-66, 1958-1 CB 60. In addition, same-sex couples who are lawfully married in the jurisdiction in which the marriage ceremony is celebrated will be considered spouses for all federal tax purposes, even if they reside in a jurisdiction that purports not to recognize same-sex marriage. *United States v. Windsor*, 133 S.Ct. 2675 (2013); Rev. Rul. 2013-17, 2013-38 IRB 201. Subsequent to the issuance of Revenue Ruling 2013-17, the U.S. Supreme Court ruled that the Fourteenth Amendment of the U.S. Constitution requires states to license marriages between two people of the same sex, and to recognize all marriages between two people of the same sex when their marriage was lawfully licensed and performed out-of-state. *Obergefell v. Hodges*, 135 S.Ct. 2584 (2015). As a result, the marriage of a same-sex couple that is lawful in the state in which the marriage was performed cannot be ignored in other states for purposes of applying their laws. The constitutional basis for this holding likely means that laws in states that purport to limit marriage to one man and one woman can never have had valid application. A discussion of this issue is beyond the scope of this paper. For convenience, some examples in this paper denominate spouses as H and W. The IRS has issued Notice 2017-15, 2017 IRB 783 which outlines procedures to allow taxpayers and executors to recalculate remaining applicable exclusion amounts and GST exemption to the extent that exclusion amounts were used or exemption was allocated by a taxpayer lawfully married to a person of the same sex who the IRS did not treat as a spouse before the *Windsor* decision was issued. Unfortunately, the procedures outlined do not address the proper re-computation of adjusted taxable gifts, so further guidance is welcomed.

[4] Prior to TCJA 2017, inflation was measured by changes to the Consumer Price Index ("CPI"), published by the U.S. Bureau of Labor Statistics. TCJA 2017 modified the index to the "Chained Consumer Price Index," ("C-CPI-U" or "Chained CPI"), which generally grows more slowly than CPI. Using CPI, the 2018 figure would have been $11.20 million instead of the $11.18 million that results from using C-CPI-U. Although many of the provisions related to individuals in TCJA 2017 are only effective for years 2018-2025, Chained CPI as the method of inflation adjustment is "permanent."

[5] The 2025 basic exclusion amount and GST tax exemption will be $13,990,000. Rev. Proc. 2024-40, 2024-45 IRB 1100.

UT LAW CLE | THE UNIVERSITY OF TEXAS | TEXAS LAW

Find the full text of this and thousands of other resources from leading experts in dozens of legal practice areas in the UT Law CLE eLibrary (utcle.org/elibrary)

Title search: Estate Planning for Modest Estates: Practical Tools Every Planner Should Know

Also available as part of the eCourse
2024 Stanley M. Johanson Estate Planning eConference

First appeared as part of the conference materials for the
2024 Stanley M. Johanson Estate Planning Workshop session
"Estate Planning for Modest Estates: Practical Tools Every Planner Should Know"