

**THE
JURIS DOCTOR
FAMILY WATCH**

**A NEWSLETTER FOCUSING ON
ESTATE PLANNING FOR
ASSET PROTECTION**

**Daniel H. McKinney & Associates
Estate Planning Group**

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ESTATE TAX REFORM UPDATE

Although the Republican Party and small business advocacy groups were successful in having a one year repeal of the federal estate tax for 2010 included in legislation in 2000, the political reality is that repeal is impossible. Small business groups once encouraged their constituents to support repeal, but studies done by the Small Business Council of America and other advocacy groups, demonstrated that the "carry over basis" rules that would operate with repeal, would cause larger capital gains taxes than would the estate tax. The estate tax always produces a tax free "step up basis" at death which is very advantageous especially with the present exemption of \$ 1.5mm going to \$ 2mm in 2006 -2008, and to \$ 3.5 mm in 2009. On the other hand, the "carry over basis" regime would always produce a capital gain tax on the increase of date of death asset value over

cost or other basis. Consequently, advocacy groups have recently indicated that small business will be better off with a larger exemption which will exclude 99.9% of small businesses without any compliance complexity. Carry over basis was tried and failed because of the impossibility of compliance with the complex accounting rules.

Curiously, now that outright repeal is blocked in the Senate by tax the rich advocates, the battle is now between what some call the "super rich" billionaires and the "merely rich" business owners. Because the powerful Senate minority in opposition will necessarily insist that the revenue be maintained, there will have to be a trade off between higher exemptions and higher rates vs lower exemptions and lower rates. Small business advocates urge a \$ 10mm exemption that would eliminate

99.9 % of their constituents from the estate tax. The super rich want \$3.5 mm exemption and a reduction in the top estate tax rate from 47% to 15%. After all, the \$ 10mm exemption means little to a billionaire. However, 99% of small business would be untouched at an exemption of \$ 3.5mm and 99.99 at \$ 10 mm.

Thus the most visible antagonists in this curious battle are the numerically small super rich and the merely rich. But the real combatants who have already won the repeal battle, are the numerically superior have nots who have every interest in maximizing revenue from all the rich, defined simply as anyone with any wealth at all. And not surprisingly, siding with them are the economically powerful multi billion dollar a year life insurance and estate planning industries which are vehemently opposed to any repeal or increase of exemptions.

THE SIX RULES FOR LAZY INVESTORS

Contributor
Michael Yerkes, CPA

Everybody provides investment advice - from your friends at the country club to your hair stylist. With over 10,000 mutual funds and about 30,000 stocks being scrutinized to the molecular level by newspapers, magazines, cable TV, radio and the internet, the noise rivals the Big Bang. My personal goal is to sift through this chatter in deference to a true fundamental long-term perspective. .

Paul B. Farrell wrote a MarketWatch Update of April 3, 2005 that was short yet extremely poignant.

1. Live below your means & save 10%.

In "The Millionaire Next Door," Tom Stanley and Bill Danko propose: being frugal is the cornerstone of wealth-building.

2. Swing for singles & bet on every horse.

Lazy investors win by being average. Successful investors know they can't always pick the right horse. What do they do? Simple: They pick every horse." (Those are simple words for diversification)

3. Trust the explosive power of compounding.

Albert Einstein put it very simply: "There is no greater power known to man than compounding interest." Compounding is more powerful than nuclear energy. (That's code for start saving now)

4. No market timing, no day trading.

Markets are random and unpredictable says Wharton economist Jeremy Siegel, The more you trade, the higher your taxes, expenses and transaction costs.

5. Buy quality and never sell.

Buffet was once asked about his favorite holding period. "Forever," said the sage of Omaha, who added that the best time to sell is "Never!" Okay, there are some exceptions but buy and hold is the way to go.

6. The tortoise always beats the hare.

In researching 5,000 millionaires, money manager Ric Edelman discovered that they average six minutes a day on personal finances. Since millionaires spend six minutes a day on personal finances that leaves 23 hours and 54 minutes for everything else.

Matthew A. Yerkes is a CPA and registered Fee-Only Investment Advisor. He does not sell life insurance, mutual funds or similar products and was formerly with Deloitte Touche and PNC providing tax planning services. Matt assists clients with investment, estate and income tax planning and will meet with you to discuss your needs without obligation.

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WITHDRAWALS FROM PENSION PLAN TO PAY MEDICAL EXPENSES MUST BE SAME YEAR PAID

Mrs. Kimball withdrew \$17,222 from a retirement plan in order to pay for her medical treatments which started in 2000 but which were mostly paid for in 2001. On her tax return for 2000, Mrs. Kimball listed the distribution but did not report the penalty or claim a deduction for medical

expenses. In 2001, Mrs. Kimball paid \$16,252 in medical expenses and took a medical deduction of \$8,724, the amount that exceeded 7.5% of adjusted gross income.

A 10% penalty is imposed on early distributions before age 59 from (cont'd p.3)

a qualified retirement plan unless the distribution falls under a statutory exception for medical expenses paid during the year of distribution limited to the amount which qualified for the medical deduction in excess of the 7.5% Schedule A offset.

Mrs. Kimball claimed that the full distribution was used to pay medical expenses and, therefore, was exempt from the 10% penalty.

The IRS, however, allowed only the excess over the AGI 7.5% offset paid in the same year as the distribution.

Unfortunately for Mrs. Kimball, the tax court agreed with the IRS. The language of the statute

clearly states that the exemption was unavailable to the Kimballs in 2000 because they did not pay any deductible medical expenses during that year. Nor was it available in 2001 because that was not the year of the distribution. *

(Kimball v. Commissioner of Internal Revenue, T.C. Summary Opinion 2004-2)

**Even if the distribution had occurred in 2001, the only amount of the distribution to escape the penalty would have been the amount of the deduction or \$8,724.*

PROPOSED CHANGES TO LAW WOULD PROTECT SPOUSE FROM BEING DISINHERITED

Under Ohio probate law, a surviving spouse can elect to take under or against the will of the first spouse to die. By electing under the will, a spouse will inherit only what the will provides. By electing against the will, a spouse will inherit an amount equal to what he or she would have received had the spouse died intestate, i.e., without a will.

If a person dies intestate, the surviving spouse will inherit 100% of the estate if there are no children or if all of the children of the decedent are also the children of the surviving spouse. The surviving spouse will inherit less if there are children from a prior union.* The election can only be made from probate assets.

Because the current law only permits spousal election from probate assets, it allows a person to effectively disinherit a spouse by placing property in a revocable or other trust which becomes irrevocable on death, by keeping separate property separate, by placing property in transfer on death or payable on death accounts, and by transferring property to others for less than fair market value. However, this is going to change very shortly. Under proposed changes, property available if a spouse elects to take against the will, would be from the new "augmented" estate rather than the probate estate.

Roughly defined, the augmented estate, is the federal taxable estate of both the deceased and the surviving spouse at the time of decedent's death plus all decedent's transfers for less than fair market

value for two years prior to death, less the separate property of both spouses and the marital debts of both spouses. The elective share would be one half of this amount.

The elective share is also satisfied by the value of marital and separate property already received from decedent as well as other property received such as the family allowance or a motor vehicle. After receiving this property, any shortfall would be satisfied first from probate assets, then from certain trust assets, and finally from other nonprobate assets.

The intent of the bill pending in the Ohio legislature is to give a surviving spouse one-half of the value of the net marital property of both spouses. Disinheriting the spouse will become very difficult in Ohio. However, there are other states that will allow it and locating assets there in trusts or banks will probably become popular.

** If there is a spouse and one child of decedent of whom the surviving spouse is not the parent, surviving spouse receives first \$20,000 plus one half of the balance of the estate with the remainder to child. If there is a spouse and more than one child the spouse receives the first \$60,000 if spouse is parent of one but not all children or first \$20,000 if spouse is parent of none of children, plus one-third of the estate with remainder to children in either case.*

**DANIEL H. MCKINNEY AGAIN NAMED CINCINNATI SUPER LAWYER
BY LAW AND POLITICS AND THE CINCINNATI MAGAZINE**

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Linda S. Bolin practices Medicaid, long term care, business, probate, health, and elder law. She is vice-chair of the elder law committee of the Cincinnati Bar Association, and has served as vice president of the Chase Women's Law Caucus, president of the Dallas Metro Counseling Association and trustee of the Cincinnati Arts Consortium, the Sarah Center, and the Terrace Guild. Previously, she was a city planner and director of planning for the City of Cincinnati Health Department.

Robert Herzog is a 2002 graduate of the Salmon P. Chase College of Law and a member of the Ohio, Cincinnati, and American Bar Associations. Mr. Herzog's focus is in the area of Probate and Estate Planning. He is also a correspondent for WB64 TV.

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