

## PRACTICAL PLANNER NEWSLETTER

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## PLANNING POTPOURRI

**Payroll Tax Audits:** Detailed federal employment tax audits will begin in November and will focus on: (1) worker classification (employee vs. independent contractor); (2) fringe benefits; (3) officer's compensation; and (4) reimbursed expenses. Don't wait to get tagged, review your policies and procedures now. Review employee classification and correct any inappropriate treatment of employees as independent contractors. Corroborate the legitimate classification of appropriate workers as independent contractors (e.g. document relevant facts, collect business cards, advertisements, etc.). In closely held businesses have your CPA confirm the reasonableness of salary. If you're underpaying salary to avoid payroll tax in an S corporation, that could be an issue. Be sure business expenses are properly corroborated and that firm policy requires

appropriate recordkeeping and reporting.

■ **Deductions and Employee Status.** A surgeon was held by the court to be an employee, not an independent contractor. So what? His business expenses were itemized deductions only deductible as unreimbursed employee business expenses on Schedule A, not as a business expense on Schedule C. See IRC Sec. 62. These are subject to the 2% floor on miscellaneous itemized expenses – i.e., they have to exceed 2% of adjusted gross income ("AGI") to be deductible. IRC Sec. 67. No surprise, they didn't so the entire deduction was lost. Maimon, TC Summary 2009-53. Here's some of the facts: ■ He executed an employment agreement expressly identifying him as an "employee". He should have signed a consulting agreement stating he was a contractor. ■ He served as an officer and director of the employer/corporation. Bad move. ■ He was

reimbursed for CME, hospital staff dues, professional societies, professional publications, and other professional expenses in accordance with policies established by the employer. Contractors should have the risk of economic loss. If many costs are reimbursed, the risk of loss is mitigated. ■ He received Form W-2 for "Wages, tips, other compensation". He should have been given a 1099. ■ He did not pay self-employment tax. You can't have your cake and eat it too. ■ He did not receive compensation from any other source, and he did not perform medical services for a fee outside of his relationship with the employer. A contractor holds himself out to others for similar



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# PRACTICAL PLANNER

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## MISTAKES PHYSICIANS MAKE

**Summary: "What's up Doc?"** What are some of the common planning mistakes many physicians make? Here are Bugs' top votes:

✎ "I won't get sued for more than the limits on my malpractice policy." Wishful thinking, but it won't keep Lord Voldemort, Esq. at bay. Not only was there never merit to this, there are cases confirming that Plaintiff's recoveries are not limited by your coverage.

✎ "I put all my assets in my spouse's name. I'm safe." Good plan but you missed the Sesame Street episode on the letter "D". Divorce!

✎ "I'm not worried about [protected against] malpractice." Yeah, but that's not the only risk. If your son has a beer bash while you're away that gets out of control how much might the lawsuits cost? A physician was on vacation with his wife. She imbibed a bit too much when out with her friends and drove over a line of children waiting for a school bus. At least it solved their estate tax problem!

The median family net worth is about \$60,000. \$2.5 million puts in you in the wealthiest 1%. When Willie Sutton, the famous bank robber, was asked why he robs banks he retorted "Because that's where the money is at." Your wealth alone may be a magnet for lawsuits. It's not only about malpractice, Doc.

✎ "I need to have an offshore asset protection trust." Great plan if it's right for you: \$5-10 million investment assets really offshore. It should only be used for a portion of your assets (a nest egg). \$25,000 - \$50,000 initial costs, and annual filings and fees. Should only be done if all other techniques appropriate to your situation have already been implemented. Do it wrong and you could be getting free government room and board until you repatriate the assets you transferred. "You can paint it any color, so long as it's black." Asset protection isn't like Model-T's, you need options.

✎ "I paid an attorney to protect my assets; I don't need to do anything else". You're still looking for the magic bullet – they don't exist, not even at Hogwarts. Any technique that might help you requires your continued effort

and involvement. If your accountant isn't involved it won't work. Every trust and entity requires annual tax filings. Every trust and entity must have proper recordkeeping to be respected. That means more cost, time and complexity. Your insurance consultants must be involved. Life insurance is a powerful asset protection tool. Property and casualty insurance are important too. Assuring that each asset and business is properly insured (and that the insurance reflects the proper trust, LLC, PC and other

entity that owns the assets) is a critical first line of defense to all sorts of claims. You cannot plan without your insurance advisers involved. Follow through is important. If you set up a trust and don't monitor it, it's useless.

✎ "Investment planning – I can do better than those fee only folks." The stats say you're way wrong. But a good wealth manager is an integral part of your asset protection team, not just an ETF picker.

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## CHECKLIST: LATE DECISIONS

**Summary: "OK mom, I'll get to it!"** Procrastination is common for more than just the teenager requested to clean up his room. What really vital planning decisions are you putting off?

✓ **Signing a living will.** Clarify what your end of life wishes are and tell your loved ones how you feel. How many people sign them in the ER on a quick form? Everyone remembers the Terri Schiavo tragedy. Don't have your end of life wishes violated because you didn't communicate them. Example: You have ALS and want every measure taken to prolong your life, including a respirator, so long as you are

of sound mind. Knowing many standard forms might restrict this you opt for a special living will that you tailor to address your special health situation.

✓ **Rebalance your portfolio regularly.** "I'll wait until the market recovers." Yeah, that's exactly why the average individual investor earned about 4% in mutual funds over the past 20 years when the return of those funds over the same time period was closer to 12%. Rebalance regularly.

✓ **Tell your loved ones that you love them.** Write an "ethical will" or heartfelt letter expressing how you feel and

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...MISTAKES PHYSICIANS MAKE

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Which entities should own which assets and how can overall family asset allocation goals be achieved. Another spin. How much did you lose in the 2000 or 2009 meltdowns? Investment risk is as real as malpractice risk. Bottom line – you need a team of advisers and your plan must be coordinated.

“I don’t have enough assets to worry about planning.” Yes, you do: Planning, to be successful, has to be implemented well in advance of any claim. The time to start planning is yesterday. If you wait until you have “enough” assets (when is that?) it’s too late. You don’t have to spend \$50,000 for an asset protection plan. The plan should be tailored to your specific circumstances. If your asset base is limited, you shouldn’t ignore planning, you should engage in planning appropriate for your circumstances. It’s not only about

your assets. If your parents intend to leave you assets, you should plan for those assets too (an inheritor’s trust).

“It’s too expensive to do.” The costs, relative to your malpractice premiums or potential losses are probably modest. You can and should undertake planning in distinct phases or steps. Not only is it more cost effective, but it makes it simpler to understand and implement. Addressing planning in phases will improve your chances of success. Doing the kitchen sink might be too costly.

“Asset protection is about protecting my home and investments, it has nothing to do with my practice.” Well, Muggle, you seem to be missing things that are clear as day to a wizard. The safer you run your practice, the less your asset protection plan will have to be tested! If you have a professional corporation for your practice, be certain it adheres to all corporate formalities. Examples: Adequate capitalization (watch accounts receivable factoring and other techniques if applied in excess), annual meetings, signed minutes, signed and implemented shareholders’ agreement (an agreement with provisions that are ignored demonstrates a lack of adherence to corporate formality), signing documents properly (in the name of the entity by an authorized officer), and so forth. Remember, the proper use of a professional entity will help insulate you from claims against other physician shareholders or members.

“I want the Whipple Procedure of asset protection planning!” Medicine and law are practiced quite differently. Docs like giving procedures and equipment special names. In estate and asset protection planning cutesy names usually mean a marketing gimmick, not a good planning tool or the sign of a renowned practitioner. It’s just different. Even Elvis says you’re barking up the wrong tree! If a plan-

ning technique has a fancy name, and especially if it has a trademarked name, don’t do it without clearing it with a reputable team of practitioners. Example: When establishing a charitable remainder trust (CRT) many advisers recommend a “wealth replacement trust.” It’s really just an

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insurance trust with a fancy name. While it’s a great technique in the right circumstances it’s not appropriate for everyone, and the fancy name should make you suspicious. Hire a good CPA, attorney, insurance consultant, and financial planner, that understand asset protection planning, not someone who specializes in planning for physicians. You want skilled practitioners, not a person skilled in marketing to physicians.

“A FLP will protect my assets.” You need to understand some core concepts. “Inside liability” is the liability associated with a particular asset. Example: You own rental property. If a tenant sues, that’s inside liability associated with the investment. Have the rental property owned by a family limited partnership (“FLP”) or limited liability company (“LLC”) to prevent “inside” liability from reaching other assets, such as your home. “Outside Liability” is created by an asset or activity other than the asset/activity in question, and from which you need to protect that asset. Example: You want to protect your rental property from malpractice. If your rental property is owned by an LLC a malpractice claimant that obtains a judgment should

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...CHECKLIST: LATE DECISIONS

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your concerns and wishes for family, friends and loved ones. Too often people literally wait until they are on their death bed and then don’t have the strength or mental presence to do so. Example: Your daughter has early onset Alzheimer’s disease. You opt to leave more in your will to a trust for her and if she dies to her husband, then to your other children. You write a letter explaining why you are leaving her more and assuring your other children it is not because you love them less. The fuzzy stuff is important too!

Protect your assets. It’s too late when you’re sued. Buy insurance and take other appropriate steps to protect your assets before a problem arises. Example: If you’re in business and subject to liability exposure, perhaps your savings should be in your spouse’s name.

Update your will. Adjust for new laws, changes in asset values and personal matters. Example: Your son has multiple sclerosis and had to leave his job, and is struggling to make ends meet. Your daughter is still getting by. Do you leave him more? Example: Your child has substantial health issues – if he/she receives government aid you might need to leave bequests in a special needs trust so you don’t disqualify him/her for government programs.

Sign a power of attorney. If you become disabled and have not taken precautions, a family member may have to petition a court to be appointed guardian to handle legal, tax and financial matters for you. That is costly, time consuming and all public record. Plan ahead.

Buy life, disability or long term care insurance. “I’ll get to it, but I’m young [healthy]...” Ask anyone diagnosed with cancer if they received a phone call in advance of the diagnosis so they could buy insurance. Health problems are equal opportunity employers and you never know when they will come knocking.

If coverage makes sense get it. There are ways to tweak coverage to keep the costs down, but to still have it in place. Example: Buy term insurance with a conversion feature. You can convert at a later date. Buy a disability policy with a longer waiting period. Buy long term care insurance while it is affordable, before you face health issues.

Maintain a calendar. “I’ve never been audited, I’ll get to it.” Not corroborating business, travel and entertainment and other expenses won’t bode well on an audit. A calendar documenting key data is easy to maintain and can be essential to address a range of tax audit issues. Are you a resident in a high or low tax state? Calendar travel dates to prove the time periods in each. Need to al-

locate earnings between states? Calendar where you worked. Claiming travel, entertainment or meal expenses? Document when, where, who and what on a calendar. Often, adding simple notations to the appointments you keep on your regular calendar take little additional time but may assure ready access to information to support a tax position. Making those entries contemporaneously gives them more credibility. Issue Crummey Powers. Yes, they should be issued by the trustee of your trusts as soon as possible after you make a gift to the trust. These notices inform trust beneficiaries of a limited right to withdraw funds from a trust thus allowing your gifts to the trust to qualify for the annual gift tax

RECENT DEVELOPMENTS

**Partner’s Inheritance Rights:** NY recently recognized a right in a same sex partner to inherit. In the recent case, the Court recognized the validity of a same-sex marriage between two New Yorkers conducted in Canada. Matter of the Estate of H. Kenneth Ranftle, File No. 4585-2008 (N.Y.L.J., Feb. 3, 2009). The Court acknowledged that a person may provide for his or her same sex spouse to inherit his or her estate just as any spouse. The deceased partner's family members should not have legal standing to object to the will. This case extends the concepts of an earlier NY case in which the court held that a marriage that was valid under the laws of Canada, Massachusetts or any other state where it was legal, was entitled to recognition in New York. Martinez v. County of Monroe.

**Split Dollar and S Corporations:** “Make a new plan, Stan...” Your family record company, an S corporation, and your life insurance trust (“ILIT”) create an agreement to own a large permanent life insurance policy on your life. Your ILIT pays for the economic benefit of the insurance and your S corporation pays for the bulk of the premium. If you get hit by the bus, Gus, the ILIT collects the death benefit and reimburses the S corporation for the premiums it advanced, or the cash value of the policy on death if greater (not the facts in this ruling). Split-dollar can be cool. But what about the tax requirement 1361(b)(1)(D) that an S corporation can only have one class of stock? All shares must have identical rights to distribution and liquidation proceeds. The key to avoiding problems, Lee, is that the ILIT must pay its fair share of the insurance cost (as determined under the split-dollar Regulations). Then no special benefit is provided to a shareholder that could violate the one class of stock rules. PLR 200914019. Reality, if you have a health issue the actual cost of insurance could be much greater than the imputed cost and a split-dollar plan, Stan, could result in a real disproportionate benefit, but no tax problem. PP