CASE 4

Clara Morrish

Today is January 1, 2009. Clara Morrish has come to you, a financial planner, for help in developing a plan to accomplish her financial goals. From your initial meeting together, you have gathered the following information.

Personal Background and Information

Clara Morrish (Age 69)

Clara is a retired homemaker. She is a recent widow. Clara's 70th birthday will be April 1, 2009.

Tim Morrish (deceased)

Clara was married to Tim Morrish, who died November 1, 2008, at the age of 69, after a brief battle with cancer. His date of birth was June 1, 1939.

Tim's estate is in probate. Tim was employed 45 years as a supervisor at ABC Co., Inc. (ABC) before retiring at age 65.

The Morrishes

They were married 50 years. Clara's health is fair.

The Morrishes' Children

Clara has two children from her marriage to Tim: George (age 50) and Vince (age 49). George and Vince are each married, healthy, employed, and self-sufficient.

The Morrishes' Grandchildren

George and his wife, Kathy, have one daughter, Sarah (age 18). Sarah is currently a senior in high school and will be a freshman at a university in September. The cost of tuition for the university is currently $20,000. Clara would like to pay Sarah's tuition for this year. As a graduation gift, Clara is paying for Sarah's trip to Europe this summer. The cost of this trip is $3,000.

Vince and his wife, Laena, have one son, Kirby (age 17). Kirby is a junior in high school. Kirby is in need of orthodontic work that will cost $6,000. Clara would like to pay for Kirby's orthodontic work. Clara is also considering gifting stock worth $9,000 to Kirby.

Personal and Financial Objectives

1. Clara wants to have sufficient income at retirement ($30,000 per year in today's dollars including Social Security benefits).
2. Clara will consider acquiring a smaller residence.
3. Clara wants to explore long-term nursing care alternatives (annual cost in today's dollars $40,000).

STATEMENT OF FINANCIAL POSITION
Tim (deceased) and Clara Morrish
As of January 1, 2009

	Assets[1]		Liabilities and Net Worth	
	Cash and equivalents		**Liabilities[2]**	
CP	Cash	$ 25,000	Credit cards[3]	$ 20,000
CP	Savings account	20,000		
	Total cash and equivalents	$ 45,000		
	Invested assets			
H	Stocks[6]	$ 20,000	***Total liabilities***	$ 20,000
CP	IRA - Clara's	40,000		
CP	IRA - Tim's	50,000		
CP	Pension[7]	150,000	**Net worth**	$ 980,000
	Total invested assets	$ 260,000		
	Personal use assets			
CP	Primary Residence[4]	$ 400,000		
W	Vacation Home[5]	200,000		
CP	Auto	18,000		
CP	Furniture and personal property	77,000		
	Total use assets	$ 695,000		
	Total assets	$1,000,000	**Total liabilities and net worth**	$1,000,000

Notes to financial statements
[1]Assets are stated at fair market value.
[2]Liabilities are stated at principal only as of January 1, 2009, before January payments. All liabilities are community property.
[3]Interest rate 18.3%.
[4]The primary residence was originally purchased for $110,000. There have been no additions or upgrades.
[5]The vacation home was inherited by Clara from her mother. Adjusted taxable basis is $125,000.

[6]Inherited from a sibling.

[7]Present value of Tim's pension

Other notes to financial statements
The $200,000 ILIT is the separate property of Tim. The income beneficiary is Clara. Remainder beneficiaries are the grandchildren. Clara has general power of appointment over trust assets. The trustee has power to invade for the health, education, maintenance, or support (HEMS) for the grandchildren. The ILIT is not listed on the Statement of Financial Position.

Title designations:
H - Husband
W - Wife
CP - Community property

QUESTIONS

1. What is Clara's federal income tax filing status for the years 2008, 2009, 2010, and 2011?
2. On November 1, 2009, Clara decides to sell her personal residence for the fair market value as of January 1, 2009. What will be her tax consequences? Disregard the vacation home.
3. What amount, if any, of Clara's pension annuity will be included in her gross income?
4. How should Clara report her jewelry business?
5. Ten years ago, Tim and Clara gave their grandchildren stock in a US domestic corporation that is publicly traded. The earnings have been steady but unremarkable over the years, returning dividends of about $1,200 for each grandchild last year. Because of an important advance in technology in the last year, the company is growing rapidly and in 2009 will pay about $2,100 in qualified dividends to each child. What are the kiddie tax implications of the dividends on the income of the grandchildren in 2009? To their parents (assume a marginal tax rate of 35%)? To Clara?
6. Rather than let the vacation home sit unused during Tim's last illness, it was rented to vacationers for 180 days in 2008. However, Clara used her vacation home for the last 40 days of the year after Tim's death in 2008. The only expenses for the home were utilities, taxes, and maintenance. How much of these expenses may she deduct? Where does she report the income and expenses on her tax return in 2008?
7. How much of Tim's IRA must Clara include in taxable income in 2008?
8. How much of Clara's Social Security is taxable in 2009?
9. What is Clara's taxable income in 2009?
10. Assume that in 2010 Clara decides to sell the stock she inherited from Tim that now has a fair market value of $24,000. She directs the broker to make the check payable to her sons, George and Vince, because she does not need the extra income from the sale. What are the tax consequences to Clara, George, and Vince as a result of this stock sale in the year of the sale?
11. A thief entered Clara's home while she was on vacation and stole an antique gun that had been one of Tim's treasures that he had purchased for $3,500. Unfortunately, while Clara had the gun appraised after Tim's death, she did not specifically insure it and only recovered $200 for the gun that had been valued at $4,500. How much may Clara claim as a casualty loss on her tax return this year?
12. Clara's best friend, Marlene, who is 67 and legally blind, is in poor health and has only a meager Social Security income of $6,250 annually. Clara invited her to live with her beginning January 1, 2009, and is providing more than 50% of her total support. How will this affect Clara's filing status and standard deduction in 2009?