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U C C E S S

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## How Will You Deal with Long-Term-Care Costs?

**L**ife expectancies have increased significantly and are expected to continue to increase in the future. As people age, however, they are more likely to develop conditions that limit their ability to live independently. Thus, as life expectancies increase, so does the need to make provisions for long-term-care costs. If you are wondering how likely it is that you will need to deal with long-term-care costs, consider the following:

✓ Almost 70% of those who are currently age 65 will require long-term care before they die. Care will be needed for an average of three years, with 20% requiring care for five years or more (Source: Center for Retirement Research, April 2007).

✓ Currently, the average annual cost for home care service is \$34,000 and for a private room in a nursing home is \$75,000 (Source: Center for Retirement Research, April 2007).

✓ Approximately half of private-pay nursing home patients run out of funds during their stay and must then use

Medicaid funding (Source: Center for Retirement Research, April 2007).

✓ Almost 72% of nursing home patients are women (Source: *Financial Planning*, April 2007).

✓ In 2006, approximately 20% of applications for long-term-care insurance from individuals age 60 to 69 were declined, while 42% of those age 70 to 79 were declined (Source: *Financial Planning*, April 2007).

### What Are Your Options?

Health insurance policies typically don't pay for nursing home care, while Medicare only pays for

100 days of skilled nursing home care, if admission follows a hospital stay. Medicaid pays a significant portion of all nursing home costs, but the government has enacted tougher rules to qualify for assistance. Typically, you need to deplete most of your assets before you qualify for assistance.

Many elderly individuals rely on family members for help, but the personal toll can be huge. Currently, long-term-care insurance pays a small percentage of all long-term-care costs.

In 2005, Medicaid paid 49% of all long-term-care costs, Medicare

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## Check on Lump Sums

**A**s part of the Pension Protection Act of 2006, the interest rate used to calculate lump-sum distributions from defined-benefit plans changed in 2008. Instead of using the 30-year Treasury yield, corporate bond yields are used. Since corporate bond yields are typically higher than the 30-year Treasury yield, lump-sum distributions will now be lower. This change is being implemented gradually over a five-year period, with full implementation in 2012.

If you are entitled to a lump-sum distribution, determine whether it makes sense to take the distribution in the near future. You can't take a lump-sum distribution until terminating from the company. However, if you are planning to retire in the next couple of years, you might want to calculate the difference those years will make on your lump-sum distribution. Not all plans allow lump-sum distributions, but approximately 48% do (Source: *Forbes*, 2008).

Please call if you'd like to review your options for a lump-sum distribution. ○○○



## Rolling Over Pension Plan Assets to Roth IRAs

**S**tarting January 1, 2008, the Pension Protection Act of 2006 permits proceeds from qualified retirement plans, including 401(k), 403(b), and 457 plans, to be rolled over directly to a Roth individual retirement account (IRA). In the past, the proceeds had to be rolled over to a traditional IRA and then from the traditional IRA to a Roth IRA. Guidance was recently released by the Internal Revenue Service on how to apply this provision.

The Roth conversion rules still apply to these rollovers. Thus, in 2008 and 2009, your modified adjusted gross income (AGI) cannot exceed \$100,000 to convert, not including any income resulting from the conversion. Amounts converted must be included in income if taxable when withdrawn (i.e., contributions and earnings in deductible IRAs and earnings in nondeductible IRAs), but are exempt from the 10% early withdrawal penalty. Starting in 2010, all taxpayers can convert, regardless of their income.

When converting from a traditional IRA to a Roth IRA, you cannot convert just the nontaxable portion of your traditional IRA. You must assume that a pro-rata portion of both the taxable and nontaxable funds in all IRAs are being converted. With a rollover from a qualified retirement plan to a Roth

IRA, however, you do not have to use the pro-rata rule. Thus, if a portion of your plan contains nontaxable funds, you can convert only that portion to a Roth IRA, putting the taxable portion in a regular IRA (if your plan allows you to split your funds for distribution purposes). This strategy would not require the payment of any income taxes following the conversion.

If you have some nontaxable funds in your retirement plan, but the plan does not allow split distributions, you have a couple of options:

✔ Transfer all of the funds to a regular IRA and then convert a portion of the balance to a Roth IRA. This requires the use of the pro-rata rules, so you will owe some income taxes on the conversion.

✔ Request a check payable to you. You can deposit the check and then write two checks — one to the Roth IRA in the amount of your nontaxable funds and another for the balance to a regular IRA. However, the plan will be required to withhold 20% of the taxable amount for income taxes, which you will have to provide from personal funds to keep the entire balance invested. You will then get that money back when you file your tax return.

If you transfer the funds to a Roth IRA and find out that you are not eligible to do so (this would only be a concern in 2008 and 2009), you can recharacterize the funds to a traditional IRA. The funds cannot go back to the retirement plan. A recharacterization eliminates any tax consequences from converting to a Roth IRA. You can also recharacterize if you decide you do

not want to pay the income taxes or your account value decreased after conversion, so that you owe income taxes on more than your account is currently worth. You have until October 15 of the year following the year of the conversion to recharacterize.

Nonspouse plan beneficiaries can also roll over inherited retirement plan balances to an inherited Roth IRA, even though they cannot roll over an inherited traditional IRA to an inherited Roth IRA. The rollover is only possible if the plan permits nonspouse beneficiary rollovers, and it must be a direct transfer to the Roth IRA. Once the assets are rolled over, the beneficiary must take required minimum distributions starting in the year following the original owner's death, even though it is a Roth IRA, since the beneficiary is not the owner or his/her spouse. However, the distributions can be taken income-tax free. The beneficiary will have to pay income taxes on the taxable portion of the plan assets, but he/she will be entitled to the deduction for income in respect of a decedent, which will help offset some of the cost.

Typically, a Roth conversion makes the most sense when funds will not be withdrawn from the Roth IRA for a significant length of time. Since a nonspouse beneficiary must start taking distributions in the year following the original owner's death, he/she should carefully analyze whether it makes sense to convert. The younger the nonspouse beneficiary is, the more benefit he/she receives from the conversion, since distributions are made over the beneficiary's life expectancy.

Please call if you'd like to discuss these new provisions in more detail. ○○○



## Long-Term-Care Costs


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paid 20%, individuals paid 18%, and private insurance paid 7% (Source: Center for Retirement Research, April 2007).


If your assets, not including your home, equal at least \$2 million, you can probably fund long-term-care costs with those assets, although you may not want to deplete your assets for this care. Those with very few assets will probably be covered by Medicaid. It is the people between these two extremes who should consider long-term-care insurance. This coverage may be especially important for women, who tend to outlive their husbands.


### What Should You Consider?


If you're thinking about purchasing long-term-care insurance, consider these points:


 **Purchase at a relatively young age.** You should probably purchase the insurance by the time you are in your late 50s or early 60s. After that, the premiums become much more expensive. You also run the risk that you could develop a serious health condition that would prevent you from purchasing the insurance. On the other hand, don't purchase the insurance too soon, or you could end up paying premiums for decades.


 **Check for inflation provisions.** Since you may not receive benefits for many years, and long-term-care costs have increased significantly in recent years make sure your policy has inflation protection. You can obtain simple or compound inflation protection. Simple protection increases the benefit amount by a specific percentage of the original benefit each year. Compound inflation increases the benefit on a compounded basis, so it provides substantially more protection.

 **Obtain insurance from a stable insurance company.** You want to obtain insurance from a company that is sure to be around for the long term.


 **Select an appropriate benefit period.** Many people choose a benefit period of three years, to cover the average nursing home stay. However, due to the substantial costs associated with long-term care, you may want to select a longer period. Lifetime coverage, however, probably isn't necessary. Only 1.5% of policyholders with five years of coverage exhausted their benefits (Source: *Financial Planning*, April 2007). Look for a provision where the insurer continues to pay benefits if you haven't reached the policy limit during the maximum benefit period.

 **Make sure the policy terms are reasonable.** Benefits should be paid in as many situations as possible, including skilled care, intermediate care, custodial care, home health care, and adult day care. Many people prefer to remain at home as long as possible, so make sure the policy covers a wide range of home services. Review the waiting period carefully to ensure a good balance between premium costs and out-of-pocket costs.


 **Understand the level of assistance needed to qualify for benefits.** Typically, benefits are paid when you are unable to perform two of five activities of daily living, including bathing, eating, using the bathroom, moving back and forth from a chair to a bed, and remaining continent. Typically, benefits are also triggered when a cognitive impairment, such as Alzheimer's disease, requires substantial supervision.

 **Determine how benefits are paid.** Some policies pay a set daily amount, regardless of your actual costs. This may be a good alternative if you are staying at home and want to compensate a friend or family member for

helping you. Other policies will only pay your actual out-of-pocket expenses up to a daily limit or may only pay reasonable and customary costs. Find out how you prove that you're entitled to benefits. Some plans require an in-house doctor to review your health, while other plans allow your own doctor's review.

 **Review new policy provisions.** Long-term-care policies are relatively new, so policy riders are evolving. Make sure to check out new provisions, such as the ability to combine a life insurance and long-term-care policy, an accelerated premium provision that allows you to stop making premiums after a certain number of years, or a provision that returns premiums if you die without using benefits. Also look into partnership policies, which allow you to qualify for Medicaid after exhausting the policy's benefit, while keeping more assets than normally allowed by Medicaid.

 **Consider sharing a policy with your spouse.** Some companies now offer policies that allow spouses to share policy benefits, which can operate in several ways. Spouses may take out separate policies, with a rider allowing them to use each other's unused benefits. Another alternative is to purchase one policy that both spouses can use. A third alternative gives each spouse a specified amount of benefits plus a third amount that can be drawn on by each spouse. However, be sure that one spouse doesn't use all the benefits, leaving the other spouse with no benefits.

 **Check the policy's tax status.** A qualified policy allows you to deduct a certain percentage of the premium, depending on your age, as a medical expense on your tax return. Medical expenses are deductible to the extent they exceed 7.5% of your adjusted gross income.

Please call if you'd like to discuss your options. ○○○

## Should You Pay Back Social Security Benefits?

**D**eciding when to start Social Security benefits is an important decision. While full retirement age for Social Security benefits is gradually increasing from age 65 to age 67, you can still start benefits at age 62. However, your benefit will be permanently reduced by 20.8% to 30%, depending on your year of birth. Wait until age 70, and your benefit will increase by 3.5% to 8% annually, again depending on your year of birth.


Thus, the amount of your benefit can change dramatically, depending on when you start drawing benefits. However, you can undo your decision by filing form 521, "Request for Withdrawal of Application," with the Social Security Administration (SSA). You must pay back any benefits you received, but you do not have to pay interest or inflation adjustments on that amount. The form asks for your reason for withdrawing your application, so that the SSA can assess whether you understand the implications of your decision.

When does it make sense to consider withdrawing your application? Suppose you retire at age 62 and decide by age 64 that you really don't enjoy retired life. You can pay back your Social Security benefits for those two years, work for six more years, and then reapply at age 70, receiving a

substantially higher benefit than you received at age 62.

Or suppose you retire at age 62 with reduced benefits. You didn't consider the fact that when you die, your spouse will receive 100% of your benefit provided he/she is over full retirement age. Now that you are 70, you wish you had waited for the higher benefit, so your spouse would have more income after your death. You can file the application, repay all benefits received, and then immediately reapply for Social Security benefits, receiving a much higher benefit amount.

But does it make financial sense to repay all benefits when you have received them for several years? In essence, you are purchasing an annuity with inflation protection by doing this. One way to evaluate your decision is to first determine how much your benefit will increase, including additional income your spouse may receive after your death. Then, find out how much an annuity from a private company would cost for that incremental income. If paying back your Social Security benefits costs less than purchasing an annuity, it's worth considering. ○○○



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## Quick Math

**D**on't have a calculator handy, but need a quick answer to a financial question? Here are three shortcuts:

✓ **How long will it take to double your money?** Divide 72 by your annual investment return. If you are earning 8% annually on your investments, it takes nine years for your investments to double in value.

✓ **How much does it cost to purchase an item before taxes?** Multiply the cost by 1.7 if you are in the 35% or 33% marginal tax bracket, 1.6 in the 28% tax bracket, 1.5 in the 25% tax bracket, 1.3 in the 15% tax bracket, and 1.2 in the 10% tax bracket. These numbers also factor in Social Security and Medicare taxes, but not state income taxes. So, if you are in the 28% marginal tax bracket and want to spend \$10,000 on a vacation, it will cost \$16,000 before taxes.

✓ **How much will your retirement savings grow in 30 years?** Assuming an 8% investment rate of return, add a zero to the amount. Thus, if you have \$100,000 today, it could grow to \$1,000,000 in 30 years. This is a handy way to look at whether it's worth spending money on something. For instance, the \$25,000 you spend on a car today could be worth \$250,000 in 30 years. ○○○

## Financial Thoughts

**O**nly 1% of households eligible for reverse mortgages actually have one (Source: AARP, 2008).

Working one additional year boosts annual retirement income by an average of 9%. (Source: The Urban Institute, 2008).

Over the past year, an estimated 75% of U.S. homes have declined in value, 19% increased in value, and 6%

were unchanged (Source: Zillow Inc., 2008).

In a recent survey, 28% of employed adults 45 or older said they planned never to retire (Source: Society of Actuaries, 2008).

In 1960, of those employed in nonagricultural jobs, 35.5% were in goods-producing jobs and 64.7% in service-producing jobs. In 2007, only 16.2% were employed in goods-producing jobs, while the

number in service-producing jobs rose to 83.8% (Source: 2008 Economic Report of the President).

According to a new survey, approximately one-third of workers age 55 to 64 (32%) said they postponed plans to retire due to stock market losses. Some 30% of those age 65 or older said they have been forced to put off retirement (Source: AARP, 2008). ○○○