**SOCIAL SECURITY**

One point to note is that social security elections are not a one time decision and there opportunities throughout retirement to switch between different types of benefits.

**When can an individual take social security distributions?**

Age 62- Benefits can begin at this age but benefits are reduced permanently in the range of 20-30% depending upon other circumstances. After the retirement age is increased to 67, reduction of benefits of 30% instead of 20%.

Full retirement 65-67- Retirement age for regular benefits is 65 but ramping up to 67 years old for retirees reaching retirement. Retirement age when unreduced benefits are available increased by two month per year for worker reaching age 62 in 2000-2005. Increases to age 66 for workers reaching age 62 in 2006-2016. Increases again by two months per year for workers reaching age 62 in 2017-2022. Retirement age will be 67 for those reaching age 62 after 2022.

**What are some ways to maximize social security benefits between spouses?**

**Spousal only benefits**- An individual who qualifies for both spousal and individual benefits AND who is at full retirement age can choose which benefits to collect when filing

One option is to collect spousal benefits while allowing his or her own benefits to receive Delayed Retirement Credits (DRCs)

The individual can then later file for his or her own individual benefits at a later time up to the age of 70 and claim increased benefits

Caution: In order to collect “spousal only” benefits, the individual cannot have filed for his or her own individual benefits. At any given time, only one spouse may be collecting spousal benefits.

Same logic applies for an individual who qualifies for both individual and survivor’s benefits. The individual can collect survivor benefits as early as age 60 while allowing his or her own benefits to increase and receive Delayed Retirement Credits.

Individual can then switch to his or her own benefits at a later date as late as age 70 and claim higher individual benefits.

**File and Suspend-**Allows the primary earner to delay and grow benefits at a guaranteed 8% per year while the lower earning spouse collects every month.

Primary earner files for benefits making the spouse eligible for the spousal benefits and then immediately request that the retirement benefit be suspended.

The primary earner requests to receive no checks, and that trigger the 8% growth per year.

Also allows an individual to retroactively change his or her mind about suspending and start collecting as if he or she had not suspended.

Example: If an individual files and suspends at age 66 and then decides at age 69 that he or she should have begun collecting at age 66, he or she can retroactively reverse the decision.

The individual will receive a lump sum payment of the benefits he or she would have collected without the suspension and going forward will pay monthly benefits based on beginning collection at age 66.

**Restricted Application-** This strategy can be used when there is a disparity in the earnings history of the two spouses. The lower earner files an application for retirement benefits. Then the higher earner will file a “restricted application” for spousal benefits on the spouse’s earnings record.

The higher earner then delays retirement to age 70 to get the 8% guaranteed growth.

Allows the higher earner to collect half of the spouses retirement benefits until turning 70 without adversely affecting delayed earnings.

**Widow or Widowers Strategy-** Strategy involves a widow or widower who is entitled to survivor benefits as well as his or her own individual benefits. Since survivor benefits can be collected earlier than other benefits (as young as 60) and are usually highest at full retirement age the strategy involves the widow or widower collecting survivor benefits beginning at 60 while deferring collecting individual benefits until age 70 when they are at their highest.

Allows survivor benefits to start flowing early to generate income while deferring collecting his or her own benefits until at their highest point.

**How does Social Security benefits work for someone who works while collecting benefits?**

If the individual is under full retirement age for all of 2014 and earns over $15, 480 or in the year the person reaches full retirement age he or she earns over $41,400 except that only earnings earned before the month he or she reaches full retirement age count toward the $41,400 limit. The exempt amounts increase each year.

An individual who is older than the full retirement age can earn any amount without losing benefits. Regardless of how much earnings are in the year of attaining full retirement age, no benefits are withheld for the month in which full retirement age is reached, or for any subsequent years.

For those who are working or otherwise don’t need social security benefits, these payments represent estate planning opportunities in that they can be used to fund life insurance policies or trusts.

**How do the loss of benefits work if someone earns more than the maximum allowed?**

If more than $41,400 is earned in 2014 before the month the beneficiary reaches full retirement age, $1 of benefits will be lost for each $3 of earning

If more than $15,480 is earned in 2014 by a beneficiary under the full retirement age for the entire year, $1 of benefits will ordinarily be lost for each $2 of earnings over $15,480.

**What counts as income for purposes of determining income in this case?**

Pensions and retirement income do not count as income and neither does interest and dividends from stocks and bond. A person can receive almost any amount of investment or passive income without loss of benefits.

**Are Social Security benefits subject to federal income taxation?**

If the total of a person’s income plus half of his or her benefits is more than the *base amount*, some of the benefits are taxable. Included in income here are tax exempt interest income and savings bonds.

Voluntary federal income tax withholding is allowed on benefits by submitting a W-V4.

If the only income a person receives is social security benefits, the benefits are generally not taxable and may not have to file a return.

**What are base amounts?**

$32,000 for married coupled filing jointly

$0 for married couples filing separately

$25,000 for all other taxpayers

**How much of someone’s benefits are subject to income taxes?**

It depends upon the person’s total income plus half of his or her Social Security benefits. The higher the total, the more benefits a person must include in taxable income. Depending upon the income level, he or she may be required to include either 50% or 85% of benefits in income.

If a person’s income plus half of his Social Security benefits is more than the following, up to 50% of his or her benefits will be included in his or her gross income:

$32,000 for married couples filing jointly

$0 for married filing separately

$25,000 for all other taxpayers

If a person’s income plus half of his or her Social Security benefits is more than the following base amount, up to 85% of benefits will be included in gross income

$44,000 for married couples filing jointly,

$0 for married filing separately

$34,000 for other taxpayers

Nontaxable and taxable income is included in income to limit opportunities for manipulation of tax liability on benefits.

**REVERSE MORTGAGES**

**What is a reverse mortgage?**

A reverse mortgage is a loan where the lender pays a homeowner (in a lump sum, a monthly advance, a line of credit, or a combination of all three) while he or she continues to live in the home. With a reverse mortgage, the homeowner retains title to the home. Depending on the plan, a reverse mortgage becomes due with interest when the homeowner moves, sells the home, reaches the end of a pre-selected loan period, or dies.

 Because reverse mortgages are considered loan advances and not income, the amount received is not taxable. Any interest accrued on a reverse mortgage is not deductible until the loan is paid in full. A lender commits itself to a principal amount, not to exceed 80 percent of the property’s appraised value.

 Although available through the private sector the vast majority of reverse mortgage borrowers choose to use a Home Equity Conversion Mortgage (HECM), which are regulated by the Department of Housing and Urban Development (HUD) and only available through an approved Federal House Administration (FHA) lender.

**What is their purpose? When should they be considered?**

Reverse mortgages are one way for older Americans to tap into the equity of their homes without having to sell them.

When it works well, can be a good financial solution to a troubled situation. For example, a retiree struggling with a decision to get full-time health care because of the expenses can use a reverse mortgage to provide the cash flow to help the retiree stay in the home.

**What are the characteristics of a reverse mortgage?**

* Must be 62 years old and own a home
* Retiree retains title to the house. The lender never owns the home even after you or surviving house vacates the property
* The retiree must continue to pay property taxes and insurance on the property and maintain it. If this is not possible, a special set aside from the reverse mortgage can be created. The requirement that the retiree pays taxes and insurance has not always been well understood and has led to some cases of default
* Repayment occurs when retiree or surviving spouse permanently leaves the home. Retiree or the estate must then repay the loan with private funds or selling the home. Retiree or the estate keeps any remaining funds
* Amount of funds depends upon the age of the youngest borrower, interest rate of loan and up front costs. The older the retiree the more funds can be made available
* Loan fees can be financed with little out of pocket costs
* The loan balance grows each time you access funds from a line of credit or receive a monthly payment. A monthly service fee is usually involved
* All reverse mortgages are non-recourse which means the total amount owed cannot exceed the appraised value of the home

**What is the advantage of a reverse mortgage?**

Many individuals approaching 62 have saved little for retirement and do not have much in the way of assets other than their home. This vehicle allows them to tap into their largest asset in years when they need cash.

**What are the disadvantages of a reverse mortgage?**

Reverse mortgages have grown significantly in the past years but have come under controversy mostly because of the fees lenders are charging. Recent years of declining equity in homes has made reverse mortgages more difficult to obtain.

In response to increasing criticism on up-front fees, the government created the HECM Saver option which has a cheaper up front mortgage insurance premium compared with the traditional HECM (the standard option). The trade- off is a 10-18% reduction in the maximum amount allowed on the saver option.

**What are the tax consequences of a reverse mortgage?**

Since the proceeds of a reverse mortgage are a loan, there are no income tax consequences and the interest is not deductible. The mortgage insurance premium amounts are, however, deductible as home interest by the borrower.

**LONG TERM HEALTH CARE INSURANCE**

The rise in the sale of LTC policies is not hard to understand as Americans are living longer with the very real prospect of them living beyond their retirement savings. The average daily cost of nursing home care is $200, although costs can vary greatly from state to state. Women, in particular , are concerned about not having enough money as they age.

**What are the design elements of a long-term care policy?**

Most long term health care plans are sold as tax qualified plans which means benefits are not taxable as long as they do not exceed a $340 per diem. Individuals and businesses paying the premium can take a deduction. A further deduction may be available if the premiums are funded from a health care savings account

To be tax qualified, must have a specific definition of “chronically ill”

* Inability to perform without substantial assistance at least two of six activies of daily living (ADLs) for an expected period of at least 90 days or
* Need substantial supervision because of cognitive impairment

ADL refers to:

* Bathing
* Dressing
* Eating
* Transferring
* Toileting
* Continence

**When do benefits begin?**

LTC policies require some period for the beneficiary to self-insure some number of days or month in a long term care facility. This time is the elimination period and the longer the insured pays out of pocket, the cheaper the premium. Typical EP is 90 days. Some have a waiver of elimination period if the insured opts for home care**.** The elimination period functions as a deductible

The EP must be satisfied only once in the insured’s lifetime.

**How long do benefits last?**

Benefit period is another coverage choice with the longer a policy pays benefits, the greater the premium cost.

Statistics show that the number of claims lasting longer than a three year period is low. Five or six years is the most anyone should need.

Spouses can share each other’s benefit period. If one exhausts their benefit period, the spouse can use it if needed.

**What about inflation?**

This is an important aspect of LTC design. Can be done through a guaranteed purchase option where insured is given a chance to buy higher rates on an annual basis.

Inflation riders can also be purchased which often use a 5% inflation factor.

Another option is a higher daily benefit purchase than what is today’s current costs.

**What are the disadvantages of LTC products?**

* Individual long term care insurance is expensive
* There is a possibility of future rate increases
* The policy cannot accumulate cash value
* No value added feature if the insured does not access the plan

There has been a tremendous rise in combination products as a result of these disadvantages , particularly life insurance/long term care policies and annuity/log term care policies

**How does a life insurance policy with long term care coverage work?**

The typical design pays long term care insurance benefits as an acceleration of the death benefit.

For example, the insured purchases a $300,000 death benefit. If the person needs long term care the policy will begin to advance a percentage of the death benefit each month. The insured elects the percentage at the time of application. Choice is usually one, two or three percent of the face amount.

In the $300,000 example, if the insured selected a two percent payout, the policy would yield $6,000 per month for 60 months..

If the insured dies before any long term care benefits are paid out, the beneficiaries would receive the full $300,000. Of long term care was needed, the policy would have advance that amount and is subtracted from the death amount. Either way, the $300,000 is paid out.

Usually has an elimination period of 90 days

**How does an annuity work with long term care insurance?**

Annuities and long term health care insurance address the same problem- living too long and running out of money. For this reason, annuities and long term health care insurance connect well with each other.

Client deposits a lump sum into an annuity, which functions normally, increasing according to a stated interest rate. At some point, a long term care disability is incurred. The individual begins to withdraw the money from the annuity –his own money first. When that is depleted, he begins to draw from additional monthly funds provided by the insurer to continue paying for the long term care claim.

By using his own money first, the insured creates a sizable elimination period because it will be some time before he needs to access insurer’s money. For example, a person pays $50,000 into an annuity which creates a $50,000 annuity with an additional $100,000 in long term care benefits. Once disabled, the insured $50,000 plus interest of clients money is paid first and the insurer’s $100,000 follows for a $150,000 total payout.

If not needed, the policy functions as annuity and paid income when needed giving the buyer another option and return on investment and has been very popular.

**MEDICARE**

Medicare is a federal health insurance program for persons 65 or older and for certain younger persons who are disabled. The Medicare system consists of four parts.

* Part A is hospital insurance and provides for institutional care, primarily inpatient hospital care, as well as skilled nursing home care, post-hospital home health care and hospice care. The program is financed by Social Security payroll deductions and beneficiaries share some of the costs through deductibles and co-insurance
* Part B is medical insurance and provides for physician’s services, outpatient hospital care, physical therapy and medical equipment. This part of Medicare is financed through monthly premiums and co-insurance by those who enroll as well as contributions from the federal government
* Part C is known as Medicare Advantage and provides insurance through contracts between the government and private care and fee for services organizations. Most individuals can choose between the traditional fee for services plans (Medicare Parts A and B) and a Medicare Advantage program. Enrollees in Medicare Advantage pay the Part B premium plus any premium and cost sharing from the plan itself.
* Part D is prescription drug coverage and can be purchased with a monthly premium

**Is it better to receive Medicare benefits through the original Medicare Parts A and B or through the Medicare Advantage Plan?**

A recipient under Parts A and B can go to almost any doctor, hospital or other health care provider and be covered. The recipient is charged a fee, Medicare pays its share and the patient is responsible for the balance. A Medigap policy can be purchased separately to cover or defray the costs not paid for by Medicare.

Medicare advantage plans pay the same core benefits as Medicare but usually are more inclusive and also often pay for prescription drug coverage.

A Medigap policy is not necessary under these plans and many plans prohibit them. Medicare Advantage plans are offered by private insurers and the terms are subject to the terms the insurer established. All Medicare Advantage plans have to be approved by the federal government. The premiums may be higher than Parts A and B because more benefits are offered.

Medicare Advantage Plans use managed care (PPOs, HMOs) with networked providers to control costs so an individual should first look to see what physicians, hospitals and other health care providers are in the plan’s network before deciding. A person can buy Medicare Advantage for a year or more and then return to Medicare Part A and B in a later year.

**What if the recipient is 65, eligible for Medicare and continues to work and is covered under a group health plan through his employer?**

If the recipient is covered under an employer health plan and is over 65, Medicare acts as a secondary payer. An employee is allowed to reject the employer health care plan and retain Medicare and the employer cannot have an inducement in any way to get the employee to select Medicare

**What are the limits of Medicare Part A coverage?**

* Inpatient care in a hospital is covered for up to 90 days for each benefit period. Patient pays a deductible of $1,216 in 2014 for the first 60 days and coinsurance of $304 for each day after that up to 30 days. Also a non renewable lifetime reserve of 60 additional hospital days with coinsurance of $608 per day
* Stays in a nursing facility are covered for up to 100 days in each benefit period. Patient pays nothing for the first 20 days in 2014 and then $152 per day after that. A 100 day stay in a skilled nursing facility in 2014 would cost $12, 160.
* 100 home care health visits after a stay in a hospital or nursing facility. Patient pays nothing if enrolled in Medicare Parts A and B.
* Medicare does not cover at all “custodial care” in a nursing facility. Care is considered custodial when it is primarily for the purpose of helping the patient with daily living and could be provided by people without professional skills or training
* Medicare does not cover home health care if the care is to help with daily living activities ( laundry, meal preparation, assisting in bathing, etc)

**These limitations then drive the need for long term care insurance**

**How does one enroll in Medicare Part B?**

Initial enrollment begins in a seven month calendar period which start on the first day of the third month before the individual first becomes eligible.

Can enroll later which runs from January 1 to March 31 each year with an effective date the following July 31.

If a person is eligible to enroll but does not, he will have a higher premium when he enrolls later or if he drops out and later re-enrolls. The premium will be 10% higher for each 12 month period they did not enroll.

This higher rate does not apply if the individual was covered under an empoyer health plan with Medicare as secondary payer. Those individuals will have a special enrollment period after leaving employment that last for eight months.

**What is the premium for Part B and what is covered?**

For most indiiduals in 2014, the premium if $104.90 per month and can be deducted from monthly social security premiums. There is also a deductible of $147 per year in 2014 and Medicare pays 80% of approved charges.

Outpatient mental illness services are now covered under Medicare starting in 2014.

Chiropractic and podiatrist visits are covered. Dental coverage is not part of medicare.

Home nursing care is covered if for chronic type conditions by skilled nurses and will pay for home health care after Part A coverage is exhausted. Custodial care is not covered.

Diabetes self management costs are covered

Dental, vision and wellness care can be covered under Medicare Advantage with purchase of optional coverage under one of the Advantage programs

**QUALIFIED PLANS: DISTRIBUTIONS AND ROLLOVERS**

Many clients will have substantial sums of money in qualified plans like a 401(K) and 403(b) deferred annuity plans. Rules can be very complicated on distributions and rollovers but some of the following questions can be used as a guide:

* What kinds of distributions does the plan itself provide for? In particular the summary plan description (SPD) should be reviewed to see what options are available
* Can and should the distribution be rolled over?
* If periodic payments are chosen, which payment schedule is best?
* How will payments be taxed?

What are the considerations involved with taking minimum distributions?

Minimum distributions must begin no later than April 1 of the calendar year after which the retiree attains age 70 ½ or the year after the employee retires. So, for someone who is still working past the age of 70, there is no requirement for the individual to take distributions. A participant can always take out more than the required minimum.

Under IRS regulations, the the required minimum distribution each year is determined by dividing the account balance by the appropriate number in the lifetime required minimum distribution table provided for in the IRS regulations.

For clients with substantial accumulations, it almost never makes sense to take all the money out at retirement for tax reasons.

Current rules for required minimum distributions permit significant long term tax deferral

The potential for tax deferral can extend over as many as three life expectancies. During the plan partiipant’s lifetime, minimum distributions are calculated over what amounts to a joint and survivor life expectancy in that if the participant is married and dies before the spouse, the spouse can roll the remaining balance into the spouse’s IRA and name a younger beneficiary. At the spouse’s death, younger beneficiary can continue the payments over the beneficiary’s life expectancy.

**Is it best to rollover retirement accumulations from a qualified plan into an IRA at retirement or keep it in the plan?**

There are advantages to each approach. In an IRA, there may be more investment flexibility in practice since the IRA owner is not dependent upon plan trustees and can shop for the best IRA arrangement suited for that individual.

On the other hand, loans may be available from a qualified plan that are not for an IRA. Another important consideration is that qualified plans generally offer better protection against creditors and offer more protection in bankruptcy proceedings.

**What about converting from an IRA to a Roth IRA in retirement?**

Some basic aspects of the Roth IRA must be considered:

* There is no limit on the rollover and it can be a total or partial rollover of an existing IRA
* The amount that is rolled over is included in the gross income of the IRA account holder for federal tax purposes.
* Distributions from the Roth IRA are tax free is held for five years and are made after 59 ½, death or disability

For older clients who will have to start taking minimum distributions soon, the fact that taxes will have to be paid soon on the minimum distributions ames traditional IRAs less attractive. Since no lifetime minimum distribution requirements apply to Roth IRAs, the distributions are tax free and may be deferred until death

To get the full benefit of the conversion, however, the client must pay with non IRA funds to pay the federal and state income taxes in the year of the conversion.